

January 15, 2014

IOWA UTILITIES BOARD

STATE OF IOWA
DEPARTMENT OF COMMERCE
BEFORE THE IOWA UTILITIES BOARD

IN RE: REQUEST FOR INVESTIGATION INTO APPROPRIATE AVOIDED COST METHODOLOGIES	DOCKET NO. INU-2014- 0001
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The Environmental Law & Policy Center (ELPC) and the Iowa Environmental Council (IEC) submit this Request for Investigation into Appropriate Avoided Cost Methodologies pursuant to the Joint Motion for Approval of Non-Unanimous Settlement Agreement submitted on July 26, 2013 and the Iowa Utilities Board (Board) Order issued on December 2, 2013 in Docket No. EEP-2012-0001 and the Joint Motion for Approval of Non-Unanimous Settlement Agreement submitted on August 26, 2013 and the Board Order issued on December 16, 2013 in Docket No. EEP-2012-0002

The settlement in both EEP-2012-0001 and EEP-2012-0002 included a provision with an agreement between the Office of Consumer Advocate (OCA), ELPC, IEC and MidAmerican and IPL, respectively, to request an investigative proceeding to address the issue of avoided cost in more detail. (EEP-2012-0001 Joint Settlement at p.18; EEP-2012-0002 Joint Settlement at p. 20.)

The Board approved the settlement terms. In approving the settlement terms, the Board required that,

The signatories requesting the investigative proceeding are to specify the issues they intend to address that have not already been addressed in either the tariff proceeding or the IPL/MidAmerican energy efficiency plan proceeding, specify their respective ongoing concerns, and propose solutions for discussion that would address their concerns.

(EEP-2012-0001 Order at p.66-67; EEP-2012-0002 Order at p.62-63.) In response to the Board Orders, ELPC and IEC recommend that the investigative docket address the following issues:

- Whether different avoided cost methodologies from those currently used by the utilities may be more appropriate to meet long established policy goals;
- Whether avoided cost methodologies should be more transparent; and
- Whether utilities should use the same uniform avoided cost methodology for PURPA QFs and EEP proceedings.

The INU Should Explore Alternative Methodologies with a Goal of Identifying a Uniform Methodology that is Fair and Supports the Public Policy Goals of PURPA and the Iowa Energy Efficiency Statutes and Rules.

Using a methodology that sets an appropriate avoided cost rate is important. When the IUB allows a rate that is too high, it can result in consumers paying more for the addition of QF capacity than for a utility's planned new generation. But a rate that is too low will not be sufficient to encourage the addition of QF capacity or the adoption of energy efficiency measures, even if the QF capacity and/or energy efficiency measures cost less than the utility's planned new generation. As a result, a rate that is too low can also result in consumers paying too much.

It is important that the methodology lead to an avoided cost rate that is sufficient to achieve the PURPA policy goal of encouraging the development of cogeneration and small power production and the long established Iowa policy to give implementation of energy efficiency the highest priority. 199 Iowa Administrative Code § 35.1. In addition to a sufficient rate, providing a long-term levelized rate is very important to provide potential QFs the certainty needed to invest in renewable or alternate energy technology.

A significant factor that causes confusion, lack of understanding and a perceived lack of transparency is an inconsistency between what PURPA avoided costs are supposed to achieve and what the avoided cost rates offered by the utilities signal to distributed renewable energy

developers. PURPA requires FERC to prescribe and revise “such rules as it determines necessary to encourage cogeneration and small power production.” 16 U.S.C. § 824a-3(a). But the utilities’ avoided cost rates frequently do not encourage development of QFs. For example, there are 51 wind turbine projects larger than 100 kW that are not part of a large wind farm developed using PURPA avoided cost rates. Of those 51 projects, not a single one of those projects has been developed in MidAmerican’s service territory. MidAmerican’s service territory has a good wind resource and a large number of utility scale wind farms. This would suggest that MidAmerican’s PURPA avoided cost rates do not encourage development of QFs.

FERC rules implementing PURPA, and relevant FERC orders, give states discretion on the methodology used to determine avoided costs. While there are many ways to derive avoided cost rates that meet the broad statutory requirements, there are some methodologies that will be better than others at achieving the policy goals to encourage the development of renewable energy. There are several considerations that should be reflected in any uniform avoided cost methodology. These include:

- The potential to avoid or delay the costs incurred by adding new utility-owned electrical generating capacity. Utilities are always planning capacity additions. The current activity of IPL and MidAmerican are a good example of this. The Board has recently approved IPL’s proposal for a new natural gas plant. MidAmerican is in the process of building over 1000 MW of new wind generation and has recently been exploring building both a new nuclear plant and a new natural gas plant. QF purchases and energy efficiency can help a utility avoid these capacity additions altogether in some cases or defer construction for additional years if it is not possible to avoid a unit entirely.
- Avoided environmental costs.

- Avoided transmission and distribution costs.
- Avoided line losses.
- Benefits provided by QFs and/or energy efficiency measures, such as peak load shaving or reduction (e.g., as provided by solar PV), system reliability, power quality, voltage support, fuel price mitigation, etc.

One methodology that has the potential to address many of these concerns is a proxy unit approach that focuses the determination of avoided costs on the levelized cost of a utility's next planned generating asset or on a generic generating asset, such as a combined cycle gas turbine.¹ The proxy unit approach may offer simplicity, transparency, fairness, and a rate that would be sufficient to encourage development of QF capacity and implementation of more energy efficiency.

The proxy unit approach can also develop resource-specific avoided costs, another concept worth exploring. This is particularly important for achieving fairness in the avoided cost context. For example, MidAmerican's QF tariff is just above 2 cents per kWh. Distributed renewable energy developers agree that the avoided cost rate is too low for QFs to justify investment in renewable generation. At the same time, MidAmerican has installed several billion dollars of renewable generation and is in the process of installing several billion dollars of additional renewable generation that will cost its customers much more than 2 cents per kWh. This large discrepancy between what MidAmerican offers QFs and what MidAmerican charges its own customers represents more than a return on MidAmerican's investments and raises concerns of fairness and whether MidAmerican's avoided cost rates reflect actual avoided costs.

¹ Carolyn Elefant, *Reviving PURPA's Purpose: The Limits of Existing State Avoided Cost Ratemaking Methodologies in Supporting Alternative Energy Development and a Proposed Path for Reform*, at 17 (2011). States using the proxy unit approach include Oregon, Idaho, Montana, and Utah.

In addition, the importance of having avoided cost rates that encourage the development of renewable resources has been highlighted by recent developments. In EEP-2012-0001, the Board approved IPL's discontinuance of its Efficiency First Renewable Energy Program. (EEP-2012-0001 Final Order at 34-35.) IPL noted that in the absence of the program, it would support customer installation of renewable technology through its tariff options. (EEP-2012-0001, Direct Testimony of Jeanine Penticoff at 6.) IPL's Cogeneration and Small Power Production Tariff relies on its PURPA avoided cost calculations. If that tariff is to encourage the development of renewable projects, the avoided costs must use a methodology that is fair and results in an avoided cost rate that actually encourages development of renewable projects.

An INU is the appropriate venue to fully evaluate new and different approaches to the determination of avoided costs and to ensure that the methodology applied to both energy efficiency and PURPA QF rates takes into consideration all of the necessary factors in a consistent and transparent manner.

The INU Should Address Transparency in Avoided Cost Methodology to Create a Methodology that Allows Interested Parties to Review Development and Appropriateness of Avoided Cost Rates.

A lack of transparency on how avoided costs are determined is a significant impediment to Board and third party review of avoided cost rates. The INU should explore how the utilities can use a uniform methodology that is clear, transparent, and fair – one that allows interested third parties to determine whether those rates are, in fact, just, reasonable, in the public interest, and nondiscriminatory.

The utilities use complex models with many assumptions to generate avoided costs, without providing all the underlying assumptions or explaining how those assumptions are used. The current process involves the utility resource planner making numerous assumptions that each

have an impact on avoided cost rates. Those assumptions can vary greatly from planner to planner and utility to utility. Those different assumptions are then used in different models. Third parties cannot easily determine the assumptions underlying a number of key questions, such as:

- How do the assumptions made for calculating QF avoided cost tariffs compare with the assumptions used by the utility for justifying its own investments in new generation?
- Are capacity related costs included in the avoided cost rates? If so, do they represent short-term market rates, long-term market-based rates or costs related to the utility's own actual cost for comparable generation capacity?
- If a utility has not committed to the construction of new generation, are there no avoided capacity related costs? At what stage in the planning process for the construction of new generation does that new generation get reflected in avoided costs?
- After a utility completes the construction of new generation, do avoided capacity costs become zero since a utility no longer needs more generation for at least some period of time?
- Should actual wholesale market prices be considered in setting QF tariffs since they may be quite different than the actual long-term cost of owning and operating generation?

A factor worth highlighting is the lack of transparent generation decisions. Frequently, the utilities are both publicly and privately exploring additional new generation that is not reflected in avoided cost filings. For example, MidAmerican actively explored a large new nuclear plant, is possibly exploring a new natural gas plant and is in the process of adding 1000 MW of wind generation. None of these new generation options were reflected in MidAmerican's most recent PURPA filings, but any new generation is relevant in adequately developing avoided

costs. Integrated Resource Planning would provide more transparency in utility generation decisions that can be used consistently across filings. Pieces of this information are currently required in various Board-mandated filings, including the energy efficiency filings. In addition, Alliant files an integrated resource plan in Minnesota that includes some Iowa information. A requirement for public integrated resource plans would add consistency and transparency and would make the generation information used in avoided cost models easier to understand and more consistent. A smaller step that would increase transparency is to require PURPA avoided cost filings to include the information provided by the utilities EEP filings on avoided capacity and energy costs in PURPA avoided cost filings, and in addition to that information, require the utility to provide the justification for the key input decisions and the assumptions that the planner makes.

The INU Should Explore How Use of a Uniform Methodology for Energy Efficiency and PURPA Avoided Cost Rates Will Further Transparency, Consistency and Public Policy Goals.

Under the current system, each utility uses its own methodology for determining PURPA and energy efficiency avoided costs, respectively. Moreover, these methodologies are not consistent between utility companies. ELPC and IEC believe that Iowa should move towards a uniform methodology for utility determination of both PURPA and energy efficiency avoided costs.

Importantly, this includes the use of the externality factor that captures important benefits of energy efficiency in terms of avoided environmental costs. Those environmental costs can be avoided in the renewable energy context as well and therefore should be reflected in the PURPA avoided cost rates. FERC rulings allow for externality factors reflecting environmental costs as part of avoided costs. *See California Public Utilities Commission v. Southern California Edison*

Co., Docket No. EL-1064-001 and EL 10-66-001, Order Granting Clarification and Dismissing Rehearing, at 15 ¶ 31 (FERC 2010) (“[I]f the environmental costs ‘are real costs that would be incurred by utilities,’ then they ‘may be accounted for in a determination of avoided cost rates.’”). FERC further specified that if an adder or bonus or externality factor is based on “an actual determination of the expected costs,” it is a valid avoided cost “consistent with PURPA and [FERC] rules.” *Id.*

FERC has made clear that actual avoided environmental costs can be included in PURPA avoided costs, and a uniform methodology will be able to account for environmental costs in both the energy efficiency and PURPA contexts. A thorough, transparent, and detailed examination of the actual avoided environmental costs during the INU could lead to the externality factor in the energy efficiency avoided cost rates increasing in the future and minimally would lead to accurate avoided environmental costs being incorporated into PURPA avoided cost rates consistent with FERC rulings.

Avoided Cost Methodology Docket Recommendations

ELPC and IEC recommend that the Board convene the Avoided Cost Methodology investigative docket this spring with a goal of using the 2014 PURPA Avoided Cost filings to test the ideas in this docket in a concrete and practical way and help draw conclusions about avoided cost methodologies. The idea would be to apply what is learned initially in the INU and use that information to have the utilities file PURPA avoided costs using their current methodologies and several of the alternative uniform methodologies discussed in the docket. The utilities would produce the alternative versions of their avoided cost filings using the different methodologies and would attempt to use the methodologies in the same way with a transparent set of assumptions. The parties and the board can evaluate the application of the different

approaches and use of common assumptions. This would allow for a practical evaluation of the uniform methodologies and testing of transparency principles rather than a purely theoretical exploration.

Initial comments in the spring should address uniformity of methodologies between utilities and between EEP and PURPA filings, how to make avoided cost methodologies more transparent and how current and alternative methodologies help achieve policy goals of encouraging renewable energy development and energy efficiency. A workshop could be held in the early summer to focus on the common methodologies and assumptions to use in the filings. This would allow parties and the Board to develop common understanding in advance of the filing. A neutral third party could participate in the workshop to either present on the different methodologies or facilitate selection of alternative methodologies and development of common assumptions. After the utilities file PURPA avoided cost information and rates using existing and alternate methodologies, parties could file another round of comments in the fall assessing how the different methodologies meet the goals of transparency, fairness and encouragement of renewable energy and energy efficiency.

This docket will need to be coordinated with the Board's recent initiation of NOI-2014-0001 to explore issues related to distributed generation so that there is not overlapping or redundant activity. In the Order Opening Inquiry on Distributed Generation, the Board asked for comment on issues relevant to the discussion of distributed generation including whether distributed generation is economical and whether there are policies and topics the Board should explore. Avoided cost rates will certainly be relevant to NOI-2014-0001 and stakeholders are likely to submit comments regarding PURPA broadly and avoided cost rates specifically. We suggest timing the first comments in the INU after initial comments in the NOI are submitted and

evaluated. The INU will then provide the opportunity to address a limited subset of issues of importance to that docket in a more comprehensive way. Combining the INU with the required utility PURPA avoided cost filings will also enhance efficiency and reduce potential redundancy. This should position the Board to consider avoided cost at the same time the Board is considering the results of the distributed generation Notice of Inquiry.

Respectfully submitted this 15th day of January, 2014.

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