Board Decision
Amending Above-Market Cost Policy

September 19, 2012

Summary

Amend the policy governing the determination of above-market cost of renewable energy projects to eliminate the process identified for utility-scale projects, leaving a process applicable to all projects of 20 megawatts and less in size, and make minor adjustments to account for projects that generate energy on-site, or which are processed under the utility master agreements.

Background

- The 1999 law that first authorized the collection of ratepayer funds for renewable energy projects, SB 1149, limited the use of these funds to "the above-market costs" of new renewable energy resources. The Oregon Public Utility Commission regulations define "above-market costs" as:

  [T]he portion of the net present value cost of producing power (including fixed and operating costs, delivery, overhead, and profit) from a new renewable energy resource that exceeds the market value of an equivalent quantity and distribution (across peak and off-peak periods and seasonality) of power from a non-differentiated source, with the same term of contract.

  OAR 860-038-0005(1),
  http://arcweb.sos.state.or.us/pages/rules/oars_800/oar_860/860_038.html

- In 2002, the board adopted an above-market cost policy. The policy specified a methodology for comparing the cost of a renewable resource with the market price of power, i.e., the price of non-renewable energy on the open market, using levelized present values (i.e., the total benefits of the project adjusted to remove the impact of inflation and smooth variable output).
- The methodology identified the maximum amount that Energy Trust would pay toward a project. The actual payment was to be negotiated case-by-case, based on factors such as: the costs and returns of comparable projects, the project's value in opening up new markets or demonstrating important technologies, ownership of renewable energy certificates, and other factors relating to the Energy Trust Strategic Plan.
- Before 2007, most of Energy Trust's renewable generation came from larger, utility-scale wind projects. These projects were governed by "master agreements" negotiated with PGE and PacifiCorp, which established procedures for identifying projects and negotiating funding agreements. Energy Trust's above-market cost policy described different methodologies for utility-scale projects and smaller projects.
- In 2007, the Oregon legislature limited Energy Trust funding for renewable energy projects to the costs of constructing and operating projects with a nominal generating capacity of 20 megawatts or less. Since then, the methodology for evaluating above-market costs has been the same for all renewable projects, whether utility-sponsored or not. Energy Trust and the utilities still may use the procedures of the master agreements to negotiate funding for utility-sponsored projects, but the evaluation of above-market costs does not vary.

Discussion

- The limitation on use of Energy Trust renewable energy funds to projects of 20 megawatts and less moots the policy provisions applicable to utility-scale projects. Staff proposes to remove them.
- As Energy Trust has focused on smaller renewable projects, it has dealt with more projects that generate energy for use on site. For example, net-metered residential solar projects generate energy for a home and feed the surplus to the grid. Staff proposes to clarify that Energy Trust will use the retail energy rate paid by the customer to determine the market value of on-site energy in determining above-market cost.
- Because Energy Trust continues to fund projects sponsored by utilities, staff proposes to amend the policy to reflect the fact that the procedural aspects of the utility master agreements remain in effect, and may be used in negotiating funding agreements.
- The policy committee reviewed these recommendations on September 4, 2012, and supported them.

Recommendation

Adopt changes to the Energy Trust policy on determination of above-market costs, by adopting resolution 645.

RESOLUTION 645

AMENDING ABOVE-MARKET COST POLICY

WHEREAS:

1. **Ratepayer funds for renewable energy projects may be used for "the above-market costs" of constructing and operating new renewable energy resources.**
2. **In 2002, the board adopted an above-market cost policy specifying a methodology for comparing the cost of a renewable resource with the market price of power, i.e., the price of non-renewable energy on the open market, using levelized present values.**
3. **The methodology identified the <u>maximum</u> amount that Energy Trust would pay toward a project.**
4. **Before 2007, most of Energy Trust's renewable generation came from larger, utility-scale wind projects. These projects were governed by "master agreements" negotiated with PGE and PacifiCorp, which established procedures for identifying projects and negotiating funding agreements. Energy Trust's above-market cost policy described different methodologies for utility-scale projects and smaller projects.**
5. **In 2007, the Oregon legislature limited Energy Trust funding for renewable energy projects to the costs of constructing and operating projects with a nominal generating capacity of 20 megawatts or less. Since then, the methodology for evaluating above-market costs has been the same for all renewable projects, whether utility-sponsored or not.**
6. **As Energy Trust has focused on smaller renewable projects, it has dealt with more projects that generate energy for use on site. Net-metered solar projects, which generate energy for a home and feed the surplus to the grid, are an example.**

It is therefore RESOLVED that the Energy Trust policy on above-market costs of new renewable resources is amended as shown in Attachment 1, to:

1. **Eliminate the process identified for utility-scale projects, leaving a process applicable to all projects of 20 megawatts and less in size;**
2. **Clarify that Energy Trust will use the retail energy rate paid by the customer to determine the market value of energy generated on-site; and**
3. **Recognize that the procedural aspects of the utility master agreements remain in effect, and may be used in negotiating funding agreements.**

Moved by: Seconded by:

Vote: In favor: Abstained:

Opposed: [list name(s) and, if requested, reason for "no" vote]

ATTACHMENT 1

Energy Trust of Oregon Policy: Procedures for Evaluating the Above-Market Cost of a Renewable Resource Project

~~Utility-scale Renewable Resources~~

~~The utility-scale renewable resources are identified in competitive requests for proposals and other processes. The Energy Trust will work with the utilities in the design of the RFPs and the RFPs will describe the Energy Trust's above-market payment program.~~

1. ~~**Review project proposals**: Proposals must provide the technical, resource, financial and project information and operating characteristics typical for responses to a utility-scale RFP. The Energy Trust will independently review this information. As applicable, the Energy Trust will work with the utility to seek agreement on the analytical methodologies and the assumptions about the costs, discount rates, and other key factors that affect the analyses. Staff will ensure that assumptions and methodologies align with approaches approved for utility integrated planning and OPUC rulings and will document this as part of any approval process. The Energy Trust will also work with the utility in their RFP processes as mutually agreed to review projects for above-market funding.~~

2. ~~**Independent review:** The Energy Trust will independently evaluate the projects. This review will evaluate whether the proposed costs are consistent with the usual and customary costs for similar projects, the economic and technical feasibility of the projects, and credit and other financial factors. Detailed analyses will be prepared of the net present value of the power that would be generated over the life of the project. As appropriate, the evaluation will include integration, delivery, ancillary, shaping and transmission costs, and any other relevant costs or credits. The staff will compare these costs to the utilities' market cost of electricity and calculate the net-present value of the above-market payment. For bids that do not include integration or transmission, the Energy Trust will evaluate the lowest-cost alternatives available for providing these services.~~

3. ~~**Definition of market cost**: Based on the Oregon Administrative Rules (OAR) definition of above-market cost, the Energy Trust will compare the renewable resource costs to the market value that is used by the utility to acquire non-renewable resources, provided the market value was developed using methods consistent with the utility's latest Integrated Resource Plan and the Commission-approved acquisition process. The market value will typically be an updated forward price curve or marginal non-renewable resource selected through a competitive bidding process. The market cost will be adjusted to match the expected daily and seasonal delivery schedule of the renewable resource if necessary.~~

4. ~~**Calculate the above-market cost**: The defined market costs will be compared to the delivered price for the renewable resource for each year of operation. The difference between the two will define the above- or below-market cost for that year. The net-present value for these costs over the life of the project (or the contract term in the case of a Power Purchase Agreement) will be calculated using the appropriate utility's discount rate. If the net present value is positive, then this amount would define the maximum above-market cost that the Energy Trust could pay. If the net present value is zero or less, then there would be no above-market cost payments.~~

~~**5. Payment:** The Energy Trust can pay up to 100% of the above-market cost. The actual amount of the payment is determined on a case-by-case basis after considering the amount of funding available, the funding needed to develop the project, the benefits of the project, and the potential of the project to reduce renewable resource costs, provide replicable benefits, address a resource with significant potential, or meet other considerations related to achieving the objectives of the Energy Trust Strategic Plan. If the above-market payments are made to a developer, the Energy Trust will provide information to the utility so that the forecasted utility payments to the developer do not exceed the net present value of the market cost of the power over the expected life of the project. The Energy Trust will also provide this information to the Commission. Payments may be made up-front or on a periodic basis over time based on production or other factors. Payments made over time may reflect the discounted time-value of those funds.~~

~~**Mid to Small-Scale Renewable Resources**~~

The Energy Trust will evaluate ~~medium and small-scale~~ renewable resource projects that are submitted under ~~the~~ Energy Trust programs.

1. **Review Project Proposals:** ~~The~~ Energy Trust will review the costs submitted by project sponsors. Whether through standard processes or RFPs, proposals must provide sufficient information to evaluate the project, including at least technical specifications, resource characteristics, energy delivery, integration, transmission, development timelines, operating plans, financial detail, tax benefits, risks, and personnel. ~~The~~ Energy Trust will evaluate the responses and compare these to the usual and customary costs and specifications for similar resources. For complex projects, independent consultants may be used to help with this review and due diligence. Information requirements will vary by program.

2. **Definition of Market Cost:** Based on the OAR definition of above-market cost, for projects delivering power to the utilities the Energy Trust will compare the renewable resource costs to the market value that is used by the utility to acquire non-renewable resources, provided the market value was developed using methods consistent with the utility's latest Integrated Resource Plan and the Commission-approved acquisition process. The market value will typically be an updated forward price curve, QF tariff, Commission-approved avoided cost filings, or marginal non-renewable resource selected through a competitive bidding process. The market price will be adjusted to match the expected daily and seasonal delivery schedule of the renewable resource if necessary. In the case of on-site and net metered use, the market cost will be the retail rates for the customer under filed tariffs with the OPUC.

3. **Calculate the above-market cost:** The defined market costs will be compared to the delivered price for the renewable resource for each year of operation. The difference between the two will define the above or below market cost for that year. The net-present value for these costs over the life of the project (or the contract term in the case of a Power Purchase Agreement) will be calculated using industry-standards to determine the maximum above-market payment, if any, from the Energy Trust. The Energy Trust staff will document these assumptions as part of the review and the Energy Trust's approval processes, which will include a review of what was used in the developers bid compared to what is standard in the industry for rates of return and competitive cost of capital. If the net present value is positive, then this amount would define the maximum above-market cost that the Energy Trust could pay. If the net present value is zero or less, then there would be no above-market cost payments.

4. **Payment:** The Energy Trust can pay up to 100% of the above-market cost. The actual amount of the payment is determined on a case-by-case basis after considering the amount of funding available, the funding needed to develop the project, the benefits of the project, and the potential of the project to reduce renewable resource costs, provide replicable benefits, address a resource with significant potential, or meet other considerations related to achieving the objectives of the Energy Trust Strategic Plan. Payments to applicants for projects generating for own-use may be capped at the calculated net present value when comparing the cost of the project to the proposer's retail rate, if this results in a lower above-market funding from the Energy Trust than provided in step 3 above. Payments may be made up-front or on a periodic basis over time based on production or other factors. Payments made over time may reflect the discounted time-value of those funds.

Standard-Offer Resources

The Energy Trust will have some programs that require a standard offer for all projects of a similar type. Standard offers can be necessary for market development to signal consistency for long range planning and investment, or because projects tend to have uniform costs. In such instances re-calculating the incentive for each project would be a barrier to the market development and unnecessary.

For programs that have been authorized by the board to offer a standard incentive, staff will follow the procedures outlined for mid to small-scale projects. The calculation will be based on the latest available data on average costs for projects in Oregon. This calculation will be updated at least once per year with incentives adjusted, if necessary.

Other Considerations

1. **Implementation of the Above-Market Methodology:** The procedures and analyses will determine the above-market cost based on the best information available at the time of the decision; the payment will be fixed based on this information and will not be adjusted for future changes. The Energy Trust will work with the utility and others to include the most current information in the calculation of the above-market costs.

2. **Energy Trust Payments:** The payment can be made to the developer, investors, lenders, utility or other parties. The Energy Trust may make a one-time payment, establish escrow accounts, or structure other arrangements.

3. **Modifications to the Procedures:** If the Energy Trust staff determines that these procedures hinder project acquisitions or that it could be in the ratepayers' interest to modify the procedure for evaluating above-market costs, the staff may request that the board make an exception to the procedures. Prior to doing this, Energy Trust staff will consult with the utilities, the Commission staff and, within the constraints of confidentiality and timing, also with the Renewable Advisory Council. The rationale for any case-specific modifications would be documented as part of the evaluation process for board approval.

~~3.~~4. **Utility master agreements.** Energy Trust has had master agreements with PGE and PacifiCorp for several years. These agreements were negotiated with the above-market cost methodology in mind, and are consistent with this methodology, but have somewhat different procedural requirements. If utilities submit funding requests pursuant to master agreements, those procedural terms will apply.