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## STAFF MEMORANDUM

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**TO:** COMMISSIONERS AND ADVISORS

**FROM:** BRITTANY MEHLHAFF, ERIC PAULSON, AND KRISTEN EDWARDS

**RE:** DOCKET EL17-003 - IN THE MATTER OF THE FILING BY OTTER TAIL POWER COMPANY FOR APPROVAL OF TARIFF REVISIONS TO ITS RATES FOR SMALL POWER PRODUCTION AND COGENERATION

**DATE:** February 22, 2017

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Commission Staff (Staff) submits this Memorandum regarding its recommendations for the above captioned matter.

### **BACKGROUND**

On January 17, 2017, Otter Tail Power Company (OTP or Company) filed with the Commission a request for approval of tariff revisions to its Small Power Producer rate schedules Sections 12.01., 12.02, and 12.03.

Under Section 210 of the Public Utility Regulatory Policies Act of 1978 (PURPA), electric utilities are required to purchase energy offered by Qualifying Facilities (QFs), which are cogeneration facilities<sup>1</sup> and small power production facilities<sup>2</sup>. Utilities are required to purchase energy and capacity from QFs at rates which reflect the incremental costs of energy, capacity, or both, that the utility would have incurred to generate or purchase the energy if it was not supplied by the QF. These incremental costs are termed the utility's avoided costs.

Federal Energy Regulatory Commission (FERC) regulations required states to establish standardized rates for QFs with an installed capacity of 100 kW or less. These standardized rates are included in OTP's tariff as Rate Schedules Section 12.01, 12.02, and 12.03, and were first approved in Docket F-3365<sup>3</sup>. OTP updates these rates annually. OTP currently has five customers taking service pursuant to Section 12.01.

This filing updates the energy and capacity payments and the renewable energy credits based on current data, each of which are more thoroughly explained below.

### **PROPOSED ENERGY AND CAPACITY PAYMENTS**

OTP calculates the energy and capacity payments for purchases from qualifying facilities based on its most recent Integrated Resource Plan filing and Marginal Cost Study inputs. The Company uses the

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<sup>1</sup> Cogeneration facilities are generating units that produce electricity and steam simultaneously.

<sup>2</sup> Small power production facilities have a maximum size of 80 MW and have a primary energy source (75 percent or more) of biomass, waste, renewable resources, geothermal resources, or any combination thereof.

<sup>3</sup> In the Matter of the Investigation of the Implementation of Certain Requirements of Title II of the Public Utilities Regulatory Policy Act of 1978 Regarding Cogeneration and Small Power Production

results of the Strategist resource planning model to simulate the cost of the marginal unit that a QF entity would displace. OTP stated the energy payment shows a reduction from last year’s filing due to a lower market energy price forecast and a lower natural gas price forecast, which are two key assumptions in the resource plan. OTP also stated the capacity payments show an increase in the first 60 months since the Company is reflecting the need for generation capacity in the near term.

The Rate Schedule 12.01 energy payment is based on the average marginal cost. Rate Schedules 12.02 and 12.03 energy payments are separated into on-peak and off-peak for the winter and summer periods based on the Company’s on and off-peak periods for both summer and winter defined in the tariff. The Summer On-Peak Period is defined as from 8:00 a.m. to 10:00 p.m. Monday through Friday, excluding holidays, for June 1 through September 30. The Summer Off-Peak Period is defined as all other hours. The Winter On-Peak Period is defined as 7:00 a.m. to 10:00 p.m. Monday through Friday, excluding holidays, for October 1 through May 31.

The current and proposed energy payments (¢/kWh) are:

<b>Rate Schedule</b>	<b>Current</b>	<b>Proposed</b>
Rate 12.01	3.673¢	3.271¢
Rate 12.02 & 12.03 on-peak Summer	4.486¢	4.154¢
Rate 12.02 & 12.03 on-peak Winter	4.354¢	3.783¢
Rate 12.02 & 12.03 off-peak Summer	3.093¢	2.533¢
Rate 12.02 & 12.03 off-peak Winter	3.058¢	2.458¢

A QF capable of delivering power and energy to the Company on a dependable basis would take service under Rate Schedule 12.03 and be eligible for a capacity payment in addition to the energy payments. OTP determines varying levels of capacity payments based on the length of the contract term. The Company states the proposed capacity payments show an increase in the first 60 months since OTP is reflecting the need for generation capacity in the near term, 2021. The basis for the capacity payment calculation is the costs of a generic 250 MW natural gas turbine. The expected capital costs associated with the 250 MW natural gas turbine have decreased, resulting in lower proposed capacity payments.

The current and proposed capacity payments (\$/kW) are:

<b>Contract Term</b>	<b>Current</b>	<b>Proposed</b>
60 mos.	\$0.00	\$1.04
120 mos.	\$4.88	\$3.36
180 mos.	\$6.96	\$4.39
240 mos.	\$8.33	\$5.09
300 mos.	\$9.41	\$5.66
360 mos.	\$10.37	\$6.16
420 mos.	\$11.25	\$6.63

## **RENEWABLE ENERGY CREDITS**

OTP first included Renewable Energy Credits (RECs) in the Small Power Producer Rate Schedules in 2009. RECs represent the environmental attributes associated with 1 MWh of renewable energy and are tracked by M-RETS. Since OTP is currently has a REC surplus, it sells excess RECs not needed for state REO/RES compliance. OTP calculates the REC value for these Rate Schedules based on its average actual RECs sales. The REC values proposed in this filing are based on actual 2016 transactions. The current and proposed REC payments (\$/kWh) are as follows:

	<b>Current</b>	<b>Proposed</b>
Renewable Energy Credit	\$0.001175	\$0.000520

The Company adds the REC value to the energy payment in each Small Power Producer Rate Schedule to arrive at the Base Avoided Cost Plus Renewable Energy Credit payments. If the customer sells a REC to the Company and receives a REC payment from the Company, the customer transfers ownership of the REC associated with the energy OTP receives from the customer's renewable generator. If the customer does not receive a REC payment from OTP, the customer retains ownership of the REC.

## **RECOMMENDATION**

Staff recommends the Commission approve the tariff revisions with an effective date of March 1, 2017.