

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

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Chair  
Commissioner  
Commissioner  
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In the Matter of the Petition of Otter Tail  
Power Company to Revise its Cost of Energy  
Adjustment Clause Tariff to Accommodate  
Purchased Energy from Renewable Resources

ISSUE DATE: January 13, 2005

DOCKET NO. E-017/M-03-970

ORDER TEMPORARILY ALLOWING FULL  
RECOVERY THROUGH FUEL CLAUSE  
ADJUSTMENT AND REQUESTING  
REPORT

**PROCEDURAL HISTORY**

On June 27, 2003, Otter Tail Power Company filed a petition to revise its Cost of Energy Adjustment Clause tariff to permit the Company to use the tariff's automatic rate adjustment mechanism to recover the costs of purchased power generated by the use of wind or other renewable resources. The Company's immediate purpose was to establish a recovery mechanism for the costs of a newly-executed purchased power agreement for the combined output of 14 wind turbines, expected to total some 21 megawatts.

The Company proposed to recover the full contract price of these renewable energy purchases, including portions of the contract price that might be characterized as capacity costs. It also proposed to recover the cost of all purchases, whether or not individual purchases occurred on an economic dispatch basis. Finally, the Company clarified that the petition did not apply to any renewable energy purchased for its TailWinds program, a green-pricing program whose costs are already recovered through a renewable energy rider under Minn. Stat. § 216B.169, subd. 2.<sup>1</sup>

On July 28, 2003, the Department of Commerce filed comments that recommended granting the petition in part and denying it in part. The Department recommended limiting automatic rate recovery to portions of the contract price that could not be characterized as capacity charges, and to limit automatic recovery to individual purchases made on an economic dispatch basis. The

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<sup>1</sup> *In the Matter of Otter Tail Power Company's Renewable Energy Rate Implementation Plan*, Docket No. E-017/M-01-1576, ORDER APPROVING RENEWABLE ENERGY RATE IMPLEMENTATION PLAN AND IMPOSING REQUIREMENTS (February 28, 2002).

Department also cautioned that the interrelationship between renewable energy and demand charges would be examined and resolved in an industry-wide proceeding the Commission has recently opened<sup>2</sup>, and that the issue should not be predetermined here.

On August 8, 2003, the Company filed reply comments.

On October 2, 2003, the matter came before the Commission. At that time the Department and the Company submitted a joint recommendation

On October 21, 2003, the Commission issued an Order adopting the parties' joint recommendation that resolved all issues between them. Specifically, the Commission authorized Otter Tail to recover 90 percent of its purchased power costs for the wind generation at issue through the Cost of Energy Adjustment Clause and to defer the remaining 10 percent of these costs, with the potential for later true-up. The Commission directed Otter Tail to meet with the Department of Commerce for further discussions when the Company's wind generation was fully operative and accreditation data was available from the Mid-Continent Area Power Pool. The Commission also directed Otter Tail to file a tariff consistent with its agreement with the Department and stated that it would re-examine this tariff within twelve months of the date of that Order.

On October 21, 2004, Otter Tail filed a request to recover the wind power costs deferred between October 1, 2003 and August 31, 2004 but to continue deferring 10 percent of the costs incurred thereafter until there is sufficient data to calculate a capacity component.

On November 19, 2004, the Department filed comments recommending that the Commission release none of the deferred wind power costs and continue the 10 percent deferral.

The Commission met on December 16, 2004 to consider this matter.

## **FINDINGS AND CONCLUSIONS**

### **I. Otter Tail Power's Request**

Otter Tail requested that the Commission release the 10 percent wind power costs withheld pursuant to the Commission's October 21, 2003 Order. In support of that request, Otter Tail recalled that in the earlier proceeding the Department had said the Company should be allowed full FCA recovery only if the Mid-Continent Area Power Pool (MAPP) credited no capacity value to the purchases. Otter Tail argued that since the Mid-West Independent Transmission System Operator (MISO) had not approved the Company's transmission request for the wind generated power in question until September 1, 2004, the purchase was not eligible for capacity accreditation by MAPP prior to September 1, 2004. As a consequence, the Company reasoned, no capacity value can be associated with the purchases prior to September 1, 2004 and therefore full cost recovery for the pre-September 1, 2004 purchases should be allowed.

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<sup>2</sup> *In the Matter of Detailing Criteria and Standards for Measuring an Electric Utility's Good Faith Efforts in Meeting the Renewable Energy Objectives Under Minn. Stat. § 216B.1691, Docket No. E-999/CI-03-869.*

Otter Tail did not ask the Commission to discontinue the 10 percent withholding for the wind power purchased after September 1, 2004. The Company proposed to continue to withhold from the FCA 10 percent of the cost of the wind generated energy purchases for a year or until the Company and the Department agree that sufficient data has been gathered to determine the appropriate capacity value.

## **II. The Department**

The Department disputed the logic of Otter Tail's argument that not being eligible for accreditation from MAPP for the wind generated energy before September 1, 2004 means the Company should be allowed to recover the full amount of purchases prior to that date. The Department stated that not being eligible for MAPP capacity accreditation prior to September 1, 2004 does not mean that there is no accredited capacity for the resource.

The Department recommended that the Commission maintain the requirement that 10 percent of the purchase costs be withheld for the period of October 1, 2003 through August 31, 2003 and thereafter until the appropriate capacity value has been established.

## **III. Commission Analysis and Action**

The price of electricity has historically been said to be composed of two parts: an energy charge (the value of the product itself) and a capacity charge (the value of the product being reliably available on demand). Commission rules allow the automatic recovery of the energy charge portion through the Fuel Clause Adjustment (FCA) and deny such recovery to the capacity charge portion.<sup>3</sup>

Electricity generated by wind, however, poses unique challenges to this two-component understanding. An ongoing issue since 1995 has been whether any portion of the purchase price of wind generated electricity is properly classified as a capacity charge (and, if so, how to quantify that portion) or whether the price of wind generated electricity is 100 percent energy charge.

The issue has practical implications. Commission rules authorize the automatic recovery of energy charges through the Fuel Clause Adjustment but provide no such recovery for capacity charges. Recovery of capacity charges is understood to be built into the base rates that the utility charges. Hence, if some part of the price of wind generated electricity is for capacity, allowing recovery of the full contract price through the Fuel Adjustment Clause would not only violate Commission rules, but could allow the utility to double recover that portion: once in base rates and once via the FCA. If, on the other hand, no part of the cost of wind-generated electricity is for capacity, denying the utility recovery of the full purchase price through the FCA would deny it recovery of that to which it is entitled under Commission rules.

In a recent Order involving Xcel Energy's purchase of wind-generated electricity<sup>4</sup>, the Commission summarized developments on this issue.

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<sup>3</sup> Minn. Rules, Part 7825.2600, subd. 2.

<sup>4</sup> *In the Matter of the Petition of Northern States Power Company d/b/a Xcel Energy for Approval of a Renewable Energy Purchase Agreement with Velva Windfarm, LLC*, Docket No. E-002/M-04-864, ORDER APPROVING CONTRACT AS MODIFIED, SETTING REPORTING REQUIREMENTS, AND REQUESTING REPORT ON DETERMINING THE CAPACITY OF WIND GENERATION FACILITIES (December 29, 2004), at page 4.

In 1995, after a full comment period and careful review, the Commission permitted Xcel to modify its Fuel Clause Adjustment tariff to provide for 100% pass-through of purchased wind power costs. The Commission concluded that there was no factual basis for dividing wind generation into energy and capacity components and that the most reasonable approach, subject to rethinking in light of future developments, was to treat wind power as pure energy.<sup>5</sup>

Since 1995, utilities, regulators, and accrediting agencies have gained substantial experience with wind resources. While there is still no clear consensus on the capacity characteristics of wind generation, nor on how to measure any capacity component that might exist, it is reasonable to reexamine wind capacity issues in light of post-1995 developments.

The key element cited by the Department in support of maintaining the 10 percent deferral is that it appears likely that MAPP will be accrediting a certain level of capacity to utilities that have secured electricity generated by wind. For the Department, this indicates strongly that the purchase price of wind generated electricity cannot be treated as entirely an energy cost. However, the Commission notes that MAPP has not issued its accreditation for Otter Tail. And while it has been anticipated that MAPP will accredit a capacity factor for Otter Tail's wind generation purchases, MAPP has not done so to date and there is some indication that MAPP may in fact be reconsidering its accreditation assessment model with respect to the capacity issue. This level of uncertainty regarding the MAPP accreditation reflects the lack of consensus on whether wind generation has a quantifiable capacity characteristic.

At the same time, Otter Tail has argued strongly that any "capacity" attributed to wind would have no market value since a utility cannot sell wind capacity with variable (inconsistent) energy delivery and cannot sell other capacity of the same amount since energy from that capacity is needed to backup the wind generation when the wind does not blow. Moreover, Otter Tail argued, since it is a winter peaking utility and its wind turbines shut down when temperatures fall below -24<sup>N</sup>F, it is unlikely that wind generation will be available at the time of the Company's system peak.

In 2002 prior to the Commission's October 21, 2003 Order approving the 10 percent deferral, Otter Tail and the Department reached agreement and jointly proposed to defer FCA treatment for 10 percent of the costs of Otter Tail's wind generation purchases. A major part of the rationale for doing so was to allow more time for information to develop on the question of whether there is a quantifiable capacity portion of the purchase price of wind generated electricity. Under the circumstances existing at the time, the Commission found that agreement reasonable and approved it.

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<sup>5</sup> *In the Matter of the Petition of Northern States Power Company to Amend the Terms of its Electric Fuel Adjustment Clause*, Docket No. E-002/M-95-244, ORDER GRANTING VARIANCES AND APPROVING FAC TARIFF AS MODIFIED, (September 5, 1995). See also, *In the Matter of a Petition by Northern States Power Company for Approval of New Electric and Gas Rate Books and Associated Miscellaneous Tariff*, Docket No. E,G-002/M-97-985, ORDER APPROVING NEW GAS AND ELECTRIC RATE BOOKS (February 3, 1998), incorporating that decision into permanent tariffs.

This time there is no agreement and the factual case for dividing wind generation into energy and capacity components remains no clearer now than it did then. In these circumstances, the Department's argument for continuing to impose even a partial deferral is not persuasive. The Commission further notes that public policy considerations favor development of renewable energy and auger against deferring recovery of even a portion of the cost of renewable generation when the case to do so is not clearly established.

Further, the Commission notes that in a companion case, Xcel has been allowed to recover 100 percent of purchased wind power costs through the FCA since 1995 and the Commission has recently extended that authority through June 30, 2006. In that case, the Commission stated:

The Commission will therefore ask the Department to examine and report on these issues on the basis of its institutional experience, comments from Xcel and other interested persons, and information from other organizations with expertise in generation issues, such as the Mid-Continent Area Power Pool and the Midwest Independent System Operator.

Meanwhile, the Commission will authorize 100% recovery of the costs of this generation through the Fuel Clause Adjustment through June 30, 2006, to give the Department ample time to complete its review and the Commission ample time to consider the Department's report.<sup>6</sup>

The Commission finds merit in extending the same terms to Otter Tail with respect to its wind power purchase costs.<sup>7</sup> Full recovery via the FCA through June 30, 2006 will apply to the costs of the current wind project (the FPL Energy ND Wind II project) and to any other reasonable purchase of wind generated electricity that the Company makes between now and June 30, 2006. In addition, the Commission clarifies that any decision at that point that wind-generation includes a capacity component would be given future effect only. No costs recovered by reason of this Order between now and June 30, 2006 would be disallowed or removed retroactively from the Company.

While deciding not to continue the temporary 10 percent deferral at least through June 30, 2006, the Commission clarifies that it is not making a final determination in this Order that no capacity factor exists in the purchase price of wind generation. As in the recent Xcel Order, this Order authorizes full FCA recovery for a limited period, through June 30, 2006. This will give the

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<sup>6</sup> *In the Matter of the Petition of Northern States Power Company d/b/a Xcel Energy for Approval of a Renewable Energy Purchase Agreement with Velva Windfarm, LLC*, Docket No. E-002/M-04-864, ORDER APPROVING CONTRACT AS MODIFIED, SETTING REPORTING REQUIREMENTS, AND REQUESTING REPORT ON DETERMINING THE CAPACITY OF WIND GENERATION FACILITIES (December 29, 2004), at page 4.

<sup>7</sup> Xcel is subject to a legislative mandate to purchase a certain amount of electricity generated by biomass and wind purchases whereas Otter Tail has no similar mandate. This difference does not distinguish Xcel from Otter Tail on the issue of whether wind generation has a capacity component, however. Consequently, it is appropriate that Otter Tail and Xcel receive similar regulatory treatment with respect to that issue.

Department additional time to complete its review of this issue and report, prior to June 30, 2006, regarding the appropriateness of continuing to allow Otter Tail to recover 100 percent of the costs of purchasing wind-generated electricity through the FCA.

**ORDER**

1. Otter Tail Power Company is hereby authorized to recover 100 percent of the costs of the purchases from the FPL Energy ND Wind II project (and any other purchases of wind generated electricity it may make between now and June 30, 2006) through the fuel clause adjustment (FCA) until July 1, 2006.
2. Within 30 days of this Order, Otter Tail Power Company shall file tariffs that reflect the decisions in this Order.
3. The Department of Commerce is requested to prepare a report regarding the appropriateness of continuing to allow recovery of 100 percent of the costs of purchasing wind-generated electricity through the FCA and to submit it in time for Commission consideration before June 30, 2006.
4. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Burl W. Haar  
Executive Secretary

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