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Independent Power Producers Coalition - Michigan
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Statement
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Docket No. AD16-16-000

June 29, 2016, Technical Conference on Implementation Issues Under the Public Utility Regulatory Policies Act of 1978: Mandatory Purchase Obligations

Introduction:

My name is Laura Chappelle. I am pleased to be a panelist at the June 29, 2016, Technical Conference on Implementation Issues Under PURPA. I am a previous member of the Michigan Public Service Commission ("MPSC"), having served as its Chairman from 2000 – 2003, and as a Commissioner from 2003 – 2007. During my tenure at the MPSC, I was a founding member of the Organization of MISO States ("OMS") as well as the Organization of PJM States ("OPSI"). I was formerly a Deputy Legal Counsel and Regulatory Affairs Advisor to Governor John Engler, and have also served as an Adjunct Professor of Energy Law at both the Western Michigan University/Thomas M. Cooley Law School, and the Michigan State University College of Law. I am currently Counsel with the Varnum law firm in Lansing, Michigan, where I represent the Independent Power Producers Coalition of Michigan ("IPPC-MI"). My testimony today is in coordination with Dr. Kenneth Rose, who has also been advising the IPPC-MI on certain PURPA issues before the MPSC.

IPPC-MI is a group of Michigan independent power producers that operate hydroelectric, biomass, waste-to-energy, or landfill gas power generation facilities ("Facilities"), which are Qualified Facilities ("QF" or "QFs") of 20 MW or less.[1] The Facilities provide clean and renewable energy and capacity to investor-owned utilities ("IOU"), electric cooperatives, or municipal electric utilities under Power Purchase Agreements ("PPAs") in Michigan that have

[1]IPPC-MI is a coalition of Michigan independent power producers and includes among its members the following: Kent County; Hillman Power Company, LLC; Viking Energy of Lincoln, LLC; Viking Energy of McBain, LLC; Boyce Hydro Power, LLC; White's Bridge Hydro Co.; Black River, L.P.; Elk Rapids Hydroelectric Power, LLC; the City of Beaverton, and Michiana Hydroelectric Co.

been approved by the MPSC. Generally, the PPAs in question have been in existence for many years, some stretching back to the 1920s. Most of these Facilities are small in size (several under 6 MW), yet they provide reliable, distributed baseload generation and ancillary benefits to the communities in which they operate, as well as low-cost renewable energy and capacity to the electric grid. My comments today are meant to convey our strong position that the tenuous and shifting nature of state policies nonetheless continues to show that the original objectives of PURPA is as relevant today in Michigan as they were in 1978 and 2005 when Congress last amended the law. This Commission's oversight and "backstop" authority remains equally important to the QF community, especially those providers that are 20 MW and under, that simply do not have the numerous rate and interconnection protections and assurances as do most traditional electric utilities.

Comments:

Please accept these brief comments in response to the questions directly related to the panel in which I will participate, regarding Mandatory Purchase Obligations, and the Commission's regulations implementing the mandatory purchase obligation under PURPA in light of changes in the electricity markets since the enactment of PURPA.

1. **Application of the "one-mile rule," including implications of the "one-mile rule" on current electricity markets and its implications for utilities' long-range resource planning efforts.**

   The Commission's one-mile rule, established pursuant to section 292.204(a)(2)(ii), for purposes of determining the maximum size criteria of a small power production QF, has not created significant issues with Michigan's long-standing QFs of 20 MW or less. The purposes of the rule and the standards that are used in its interpretation appear to be fairly balanced and serve their intended purposes for QFs of 20 MWs or less. Therefore, the IPPC-MI does not have comments on its application at this time.

2. **The rebuttable presumption that the Commission has adopted in the context of PURPA section 210(m) that QFs 20 MW and below do not have nondiscriminatory access to competitive organized wholesale markets and the barriers to access encountered by these facilities.**

   Maintaining the rebuttable presumption that QFs of 20 MW or less do not have non-discriminatory access to competitive markets is a fundamental necessity for all of the independently-owned generators in IPPC-MI. Especially given the lack of long-term energy and capacity markets in the Midcontinent Independent System Operator ("MISO"), where the IPPC-MI members operate, maintaining section 210(m)'s rebuttable presumption continues to be crucial to the fair and non-discriminatory treatment of QFs of 20 MW or less.

   Because most of the states within MISO are fully regulated, MISO's markets have never been designed to be long-term markets to ensure resource adequacy and consequently do not fully compensate generators for resource investments. Per MISO, "the current market will continue to provide only a balancing function and will fail to efficiently support resource

investment decisions in those areas of MISO that rely upon MISO's market price signals for those decisions."[2] While Michigan currently allows a limited amount of retail choice,[3] Michigan's investor-owned utilities ("IOUs") and some electric cooperatives are predominately under retail rate regulation and recover energy and capacity costs via state-approved regulated rates. Subjecting QFs 20 MW and smaller to the MISO "market" for energy and capacity costs (as some IOUs in Michigan have proposed) is neither fair nor adequately compensatory for their operations. It is noteworthy that these same utilities have not received the requisite waivers from this Commission to require QFs 20 MW and under to rely upon those markets, so setting avoided costs at market rates would allow them to effectively ignore the lack of a FERC waiver.[4]

The fact that this Commission carefully reviews applications to terminate mandatory purchase obligations, ensuring that waivers are only granted pursuant to section 210(m) of PURPA and section 292.310 of the Commission's regulations, on a service territory basis for QFs that do, in fact, have non-discriminatory access to markets, remains a fundamental safeguard for smaller QFs. This is especially true for QFs that operate in Regional Transmission Organizations ("RTOs"), such as MISO, that do not have the structure and processes in place to fairly and effectively compensate generators for long-term resource energy and capacity needs.

3. When a QF can be curtailed.

Curtailment of QFs, especially those that are 20 MW or less, should continue to be a last resort in any utility operations. Often times these smaller QFs' fuel sources are directly linked to some other high-value process or compliance obligation, such as maintenance of river or lake water levels, destruction of a green-house gas in the case of a landfill methane to energy facility, or efficient use of biomass from timber harvest. These fuel streams are not easily interrupted. Curtailing purchase of the power sends ripples up the fuel supply chain that can have adverse impacts on the higher value process and may cause significant disruptions in the local economies. For instance, a biomass plant's source fuel may be derived from multiple suppliers that are often very small family businesses that cannot absorb an interruption in cash flow. Curtailing the physical flow of Michigan QFs, most of which are smaller, remotely located facilities, can have a disruptive effect to the local grid support they provide, including capacity and VARs. The obligated utilities often contact QFs in peak load situations for local grid support, a utility benefit that is provided by the QFs at no cost to the host utility.

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[2] MISO Competitive Retail Solution, Staff Proposal, March 18, 2016, p.2.

[3] Michigan law currently allows retail electric choice of 10% of incumbents' load. This requirement, however, may be subject to substantial changes if pending legislation passes.

[4] Detroit Edison received a waiver of its mandatory purchase obligation for QFs with a net capacity in excess of 20 MW on April 15, 2010 (FERC Docket No. QF10-2-000; QM10-2-001; QM10-2-002); Consumers Energy received a similar waiver for QFs greater than 20 MW on April 24, 2012 (FERC Docket No. QM12-3-000).

QFs 20 MW or less are often small in size due to the nature of their fuel supply. They are scaled to match the available supply and optimum transportation cost of a fuel source that is the byproduct of a higher value process. As such, they improve the efficiency of a larger process by extracting value that would otherwise be a waste. Due to their small size, they are already challenged to perform on a small scale for the same cost as a utility is paid to operate a large scale power plant, without the corresponding efficiencies of scale. To curtail them or treat them as available power would impose an additional burden and create an unnecessary hardship for the QF owner and operator, as well as the local communities and economies for which they provide the ancillary benefits I have discussed.

4. The impact of utility contracting practices on QF transactions.

While we have many issues and concerns regarding utility contracting practices with QFs, two particular areas are noteworthy for this Commission's consideration. As with most contracts, the price and term are two of the most crucial aspects in any PURPA contract. PURPA's basic principle that avoided cost rates must be just and reasonable to the electric consumers of the electric utility, but also cannot discriminate against the QF, is as important today as it was when PURPA was enacted. Increasingly, we see utilities seeking to have the regulator set avoided cost rates at the "lowest cost" source of power, arguing that the lowest cost, which is often a spot-market based rate, is equivalent to the IOU's "incremental cost" and therefore an appropriate proxy for their avoided cost. Yet these proposed "lowest cost" rates are neither compensatory nor fair to the QF, nor do they truly reflect a utility's "full avoided costs." The "incremental cost of the utility" should reflect the actual costs the utility uses when it plans to either generate or purchase for itself - without the QF and over the relevant utility planning horizon - essentially amounting to costs that reflect long-term planning and that take into account necessary capital expenditures. As MISO has stated, its current market is neither long-term, nor reflective of the necessary capital expenditures that would ensure long-term investment decisions for generators.

Financeable, long-term contracts continue to be a necessary requirement for PURPA contracts. Much as regulated electric utilities need "regulatory certainty" before they embark upon building a new generation plant, banks and other financing partners routinely require a PPA that is long-term in duration in order to be financed. A typical length for such a contract (as with requested retail regulatory rate assurances for a new generation plant) generally amounts to a 20-year term. Terms shorter in duration may be acceptable under certain circumstances. There should be little question, though, that short-term contracts, often ten years or less, are exceptionally disadvantageous to a QF. The fact that some utilities are attempting to enter into only year-to-year contracts should be a clear indication that FERC's "backstop" authority will continue to be needed to ensure the spirit and intent of the law are upheld as it relates to contractual provisions related to PURPA PPAs.

5. The impact of utility interconnection practices on QF transactions.

The IPPC-MI believes that PURPA's role in setting reasonable interconnection costs and

procedures is critical to ensure that QFs can make non-discriminatory sales of energy and capacity to IOUs. The IPPC-MI believes that interconnection costs and requirements should continue to be overseen by the state or federal regulatory authority, as applicable, to ensure that the electric utility provides reasonable, transparent rates and non-discriminatory terms and conditions for this essential service. Key to ensuring reasonableness with regard to interconnection practices is an appropriate matching of the financial modelling of a QF's supply and interconnection with the physical modeling of the energy, capacity and ancillary service benefits they provide. which is effectively a distributed generation facility. QFs are burdened with the expense associated with interconnection, dedicated to delivering energy, capacity and ancillary services, and do not receive credit representing the capital or O&M expenditures the utilities avoid by having effectively distributed generation facilities on their system.

6. The obligation to purchase "as available" power.

IPPC-MI members are all baseload providers of capacity and energy to IOUs; however, we believe that the flexibility in the current law that allows a QF to choose to provide power "as available" is necessary for certain QFs and we encourage the Commission to retain that flexibility. Certain fuel supplies traditionally tied to QFs are renewable and flow from natural resources at a rate that is variable and highly available, such as hydro and landfill gas. Because there is some variability to those types of QF fuels, "as available" power arrangements are accommodating to that natural flow of fuel.

7. The obligation to sell supplemental, standby, backup and maintenance power to a QF.

The obligation to provide supplemental, standby, backup and maintenance power to a QF is a fundamental underpinning of PURPA's requirements. These services are necessary for the efficient operation of many QFs, and the need remains to ensure that utilities do not charge discriminatorily high rates for these crucial services. This is another area where PURPA continues to provide an important safeguard to QFs that is as relevant today as it was in 1978, when PURPA became law.

While state commissions are primarily responsible for overseeing these rates and procedures, this is one area where the "backstop" at FERC remains indispensable, as small QFs often lack the resources and experience of the IOUs in state-level regulatory processes and so are often at an inherent disadvantageous.

8. The obligation to purchase pursuant to legally enforceable obligations, particularly as these issues arise in new and emerging markets.

This is perhaps one of the most important questions this Commission can ask in the context of reviewing PURPA's legally-enforceable requirements. From the IPPC-MI's perspective, the need for a legally-enforceable obligation for electric utilities to purchase QF energy and capacity remains as important and relevant today as it was in the late 1970s. This obligation should remain with the electric utility to which a QF is directly connected, but also

with any electric utility to whom electric energy and capacity can be transmitted, in accordance with Section 303(d).

Without a "must purchase" legal requirement, most independently-owned generation facilities, especially those smaller facilities 20 MW and less, could not exist. The economic incentives for utilities will encourage them to build and own all necessary capacity themselves. But at a time when capacity needs are increasing, especially in the Midwest, diverse QF facilities utilizing diverse generation resources, especially renewable energy resources, provide many ancillary benefits, some of which I discuss below. They also provide much-needed distributed, often baseload, renewable generation resources. These QFs thus not only help meet reliability needs in a cost-efficient manner, but provide numerous additional benefits that are difficult to identify and quantify in a discussion focused on setting avoided costs rates and interconnection standards. The must purchase obligation establishes a necessary legal obligation for the IOU that ensures the long-term sustainability of these QF generation projects.

Some of the ancillary benefits these QF projects provide can be seen in the following examples from four IPPC-MI members:

Kent County, one of the IPPC-MI's members, has operated an integrated solid waste management system for 600,000 residents in six western Michigan cities for over twenty-five years. While its overall capacity is not large compared to a utility's baseload plant (approximately 15 MW), its renewable, baseload capacity would provide enough renewable energy to power 11,000 Kent County homes pursuant to a 90 percent capacity factor. Kent County's facility employs 40 full-time employees with a $4.5 million annual payroll.

The Tower Kleber hydroelectric power plants in Michigan were commissioned in 1918 and 1949, respectively, and still remain important facilities in the community in which they operate. At only approximately 2 MW in size, the facilities are nevertheless a significant contributor to the local tax base and help maintain pond and lake levels for recreational use. The Kleber facility also maintains a partnership with the Michigan Department of Natural Resources and the Michigan State University in the development and operation of the Black River Lake Sturgeon Hatching Facility. This facility is a primary management tool to recover the state-threatened species in the Cheboygan River watershed.

Similarly Granger Electric operates 17 MW of landfill gas to electric QFs at a 98% capacity factor, and power over 10,000 homes, directly reducing 768,000 metric tons of carbon dioxide equivalent per year.

Finally, the Viking Energy plant of Lincoln, Michigan, is an 18 MW biomass facility that has a 97% capacity factor, utilizes 250,000 tons of wood per year, employs a total of 71 FTEs and contributes approximately $4.5 million in taxes per year. The facility plays an important role in forest stewardship (including timber management and disease and infestation controls) as well as regional grid support in the form of voltage stabilization.

These are just four of the many examples of the important role that QFs 20 MW and less provide in the state of Michigan. There is no question that PURPA's existing obligations on utilities enable these facilities to operate efficiently and cost-effectively, thus providing benefits both to the utility's customers and to the communities in which they operate. Continuation of the strong leadership and support this Commission has provided to the QF community over the past 38 years remains vital to the continued success of IPPC-MI's members.