

REPORT FROM

OFFICE OF PUBLIC ACCOUNTABILITY

Date: September 21, 2020

To: The Board of Water & Power Commissioners
Martin Adams, General Manager & Chief Engineer,
Department of Water & Power

From: Frederick H. Pickel, Ph.D., Executive Director, 
Office of Public Accountability/Ratepayer Advocate

Reference: Red Cloud Power Agreements
Agenda Item #24 for Board Meeting September 22, 2020

RECOMMENDATION

OPA recommends that the Board approve the Red Cloud Power Agreements as proposed.

DISCUSSION

1. Important Features of The Power Purchase

OPA finds that the price and other terms and conditions of the Red Cloud transactions are reasonable. The counter-party is a mid-sized supplier, and terms reflect many established industry practices.

Several noteworthy features of this procurement are:

- 1) the ability of DWP to obtain additional curtailment flexibility for a set price increase of \$1.45/MWH,
- 2) the use of a greenhouse gas price index for valuing performance,
- 3) obligations of the seller concerning disabled veterans and small business,
- 4) a point of delivery with the flexibility to manage that receipt point in the California ISO's energy imbalance market, if desired,
- 5) a price reduction in the event production tax credits increase in the future,

- 6) an option to purchase the asset 13 years after commercial operation begins and at the 20 year termination date. The termination date can be extended twice (to 25 years, then 30).

DWP relies on representations for site control of the land the project will reside on. The Seller anticipates a very high capacity factor; however, because DWP only pays for energy production received at its delivery point, estimation errors (if any) would not affect ratepayers negatively.

Note that OPA has not examined or evaluated wind studies at the project site.

DWP expects the timing of this project's wind production to be an aid to smoothing the solar portion of its resource portfolio (i.e., "integration" benefits). OPA has reviewed the DWP's modeled estimates for integration benefits. While some of the "integration" benefits of this project for DWP's system may turn out to be smaller than forecast -- if the capacity factor of the project is more like that of other wind projects -- these may nevertheless become very significant benefits (approximately \$300 million) that accelerate carbon reduction at a reasonable cost. These transactions would be reasonable in OPA's opinion even if integration benefits were non-existent or smaller, rendering this aspect of the energy production's shape "icing on the cake."

2. Options To Own The Facility: Future Procurements

OPA's prior recommendations on option pricing for ownership have not yet been incorporated into procurement practices.

OPA has previously recommended that ownership options be priced by bidding, even if the option is unique to DWP's preferences in the year of procurement, and not standardized (OPA Report of August 28, 2014, Springbok Power Purchase Agreement, p.7, the "2014 Recommendation").

At this time, OPA adds to its prior 2014 Recommendation that DWP's options, in whatever form taken at the time, always be compared to a second and required bid that includes *in the price of the purchased power* the transfer of ownership to DWP at the end of the 30 year contract term for \$1. This will ensure that savings and relative advantages that DWP's procurement method asserts have a clear and transparent comparison to no ownership and full ownership at term. By analogy, it would allow the Board to understand the differences between leasing and buying a car off the lease, as expressed in the relevant metric for power of dollars per megawatt hour.

These comparisons can serve as book-ends and allow for a more certain assessment of the reasonableness of the end result. This is so even when tax credits cannot be obtained for some option structures, like \$1 at the end of term. It nevertheless will highlight the cost savings DWP

is obtaining, while ensuring they do not miss important opportunities when the markets are changing rapidly.

Because these recommendations have been made before, OPA would respectfully request that the DWP Board require these changes to RFP's involving DWP.

3. Matters Excluded

In conducting its review, OPA has not reviewed any bids or refreshing of bids from the solicitations of SCPPA, and does not therefore have any opinion about the nature of the competitive process conducted by SCPPA. Furthermore, OPA has not provided a rate impact associated with this project, beyond providing its opinion that the procurement costs are reasonable to include in rates.

Rate impacts are speculative at this time because significant variation can occur through the exercise of flexibility provided both the buyer and the seller in these contracts. The key issue OPA has focused upon in this report is whether even lower rates (and lower procurement costs) could have been obtained, and the reasons for preferring this particular outcome that the DWP wishes to have approved.