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IDAHO PUBLIC
UTILITIES COMMISSION

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BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

WOOD HYDRO, LLC, Complainant. vs. IDAHO POWER COMPANY, Defendant.	Case No. IPC-E-20-28 COMPLAINANT'S REPLY

I.

INTRODUCTION

Mile 28 Hydro Generation Facility ("MP28") had estimated it would produce electricity when it shut down for four months for repairs, but it did not produce electricity. Idaho Power Company ("Idaho Power") contends this repair period translates into a permanent long-term curtailment in whole or in part of MP28's future estimated average annual deliveries. To the contrary, MP28 has not altered, permanently altered, or altered at all, what it estimates it will deliver.

Absent permanent long-term curtailment of estimated production, the MP28/Idaho Power agreement ("Agreement") at issue in this matter contains no penalty or liquidated damage for failure to produce the amount of energy estimated in the contract. Such negative consequences for delivery of quantities different than estimated quantities did not arise in Idaho PURPA contracts until the implementation of the 90/110 rule.

Finally, should there be a determination that MP28 somehow permanently changed its estimated annual deliveries over the long term, the monies claimed by Idaho Power are expressly liquidated damages, as labeled by the agreement between the parties. Under Idaho law, such a liquidated damage clause cannot be enforced in this circumstance. The large lump sum claimed by Idaho Power for the harms caused by the breach reflects neither a reasonable forecast of just compensation for the alleged harm, nor incapable or very difficult of accurate estimation when it occurs. This missing energy has a measurable value each second of each day of each month and, therefore, liquidated damages are prohibited by Idaho law.

II.

AGREEMENT DEFINITIONS

1.1 "ANNUAL NET FIRM ENERGY" – The amount of Net Firm Energy Seller estimates it will deliver to Idaho Power at the Point of Delivery during each Contract Year.

1.11 "NET FIRM ENERGY" – Electric energy produced by the Facility, less Station Use and less Losses, expressed in kilowatt hours ("kWh"), which Seller commits to deliver to Idaho Power at the Point of Delivery on a long-term average basis for the full term of the Agreement.

1.17 "SEASON" – The three time periods identified in Article VI.

1.18 "SEASONAL NET FIRM ENERGY" – The amount of Net Firm Energy Seller estimates it will deliver to Idaho Power at the Point of Delivery during each Season.

6.1 "DELIVERY AND ACCEPTANCE OF NET FIRM ENERGY" – Except when either Party's performance is prevented by events of force majeure (Article XVI) or otherwise excused as provided herein, Idaho Power will purchase and Seller will sell all of the Net Firm Energy and Surplus Energy.

6.2 <u>"SEASONAL NET FIRM ENERGY AMOUNTS"</u> – Based on long-term historical water flow records and long-term average energy production estimates based thereon, Seller estimates that it can deliver Net Firm Energy in the following monthly amounts:

Season 1	March	0 kWh
	April	446,515 kWh
	May	892,746 kWh
Season 2	June	927,547 kWh
	July	1,012,953 kWh
	August	985,026 kWh
	September	887,890 kWh
Season 3	October	512,497 kWh
	November	133,416 kWh
	December	0 kWh
	January	0 kWh
	February	0 kWh

6.3 <u>"ANNUAL NET FIRM ENERGY AMOUNT"</u> – The Annual Net Firm Energy amount shall be 5,798,590 kWh and shall be the sum of the three (3) Seasonal Net Firm Energy Amounts Seller specified above. At Idaho Power's option the Annual Net Firm Energy amount and the resulting Appendix D lump sum repayment amount may be adjusted based on the actual performance of the Facility.

21.3 <u>"SELLER PERMANENT CURTAILMENT"</u> – If, at any time prior to the end of the term of the Agreement, Seller permanently curtails in whole or in part it's long-term average deliveries of the Annual Net Firm Energy amount specified in paragraph 6.3, Seller shall pay to Idaho Power, as reasonable liquidated damages arising out of this permanent curtailment of Annual Net Firm

Energy deliveries, the appropriate lump sum repayment amount specified in Appendix D, multiplied by the difference in megawatt-hours between the Annual Net Firm Energy amount specified in paragraph 6.3 and the reduced Annual Net Firm Energy amount after the permanent curtailment. The Annual Net Firm Energy amount in Article VI and the resulting Appendix D lump sum repayment amount may be adjusted from time to time based on the actual performance of the Facility. The lump sum repayment amount will bear interest from sixty (60) days after Idaho Power gives or receives notice of Seller's permanent reduction of the Annual Net Firm Energy amount, until paid, at a rate equal to interest rates specified in Idaho Code § 28-22-104(2) or its successor Idaho Code provision in effect during each month of that period. For purposes of this paragraph, neither reduced deliveries of Net Firm Energy due to short-term below-normal, water conditions (paragraph 6.4) nor Idaho Power's voluntary termination in accordance with paragraph 5.2.2 shall be considered a permanent curtailment. The Parties further agree that this paragraph does not constitute a waiver by Idaho Power of its right to pursue its remedies under paragraph 21.6 or by either Party of their right to an award of pre and post judgment interest, costs and attorneys fees as permitted by law in any litigation arising out of this Agreement.

III.

FACTS

MP28 was offline for repairs during the following months it estimated it would have produced electricity: November 2018, and May to July 2019. MP28 contemplated in 1994 when MP28 went into production that it would be producing energy during those four months each year. In July 2019, MP28 notified Idaho Power that the facility would be offline until the next month, August 2019. At no time did MP28 ever indicate, nor does Idaho Power claim it anticipated or MP28 indicated that the repair period would permanently last past August 2019.

With full knowledge and acknowledgement that repairs would be complete in August 2019, Idaho Power's Jerry Jardine wrote to MP28's Ted Sorenson on August 1, 2019, that Idaho Power was invoking Paragraph 21.3 liquidated damages.[1] Ironically, the August 1 letter does not contain the word "permanent," but instead recites to the contrary:

> However, Mr. Sorenson provided documentation about the Facility repairs and replacements after the July 31, 2019, phone call and has demonstrated that the Facility is being prepared to return to service and is expected to continue to deliver to deliver the required Annual Net Energy Amount to Idaho Power for the remaining term of the Agreement.

III.

ISSUES

1. Whether the Agreement requires delivery of the Annual Net Energy Amount, which is an estimate, such that failure to deliver the estimated amount every month invokes liquidated damages.

2. Whether MP28 "permanently curtail[ed], in whole or in part its long-term average deliveries of the Annual Net Firm Energy Amount… ," by not producing for four months when Idaho Power acknowledged the repair period was neither a change in long-term average deliveries nor permanent.

3. Whether liquidated damages are appropriate when the alleged harm is failure to deliver a product that trades in a fluid, granular, instantaneous market.

IV.

ARGUMENT

Idaho Power commences answering the *Complaint* by erecting this strawman at the beginning of its argument on page 2 of the *Answer*: "Each of the projects have had extended

[1] Exhibit B to the *Answer*.

periods of non-generation constituting a permanent curtailment, or failure to deliver, their contractual Annual Net Energy."

For MP28, the "extended period" was four months of no deliveries when deliveries had been expected. The repair period was not permanent or long-term. Finally, there exists no contract to deliver the Annual Net Energy, which is an estimate, so the failure to deliver electricity for four months is neither a long term nor a permanent change to future estimated deliveries and is not a beach of the Agreement.

1. Whether the Agreement requires delivery of the Annual Net Energy Amount, which is an estimate, such that failure to do so every month invokes liquidated damages.

Paragraph 1.1 defines "Annual Net Energy" as an estimate of what MP28 will deliver annually. In the case of MP28, the estimate was 5,798,590 kWh (Paragraph 6.3 of the Agreement). Idaho Power contends that a penalty exists for failure to deliver this amount during November 2019, and May through June 2019.

The assertion that MP28 must deliver 5,798,590 kWh or be subject to penalties for permanent curtailment of long-term average deliveries conflicts with previous representations of Idaho Power concerning the operation of this type of older contract.

Idaho Power belittles MP28's recitation of Idaho Power's representations to this Commission in 2004, opining that the Commission must implement a firm energy delivery obligation through use of the 90/110 delivery band. However, Idaho Power's briefing in that case is dispositive that there is no requirement in these old contracts for developers to actually deliver energy in the amounts they estimate they will provide absent a permanent curtailment of long-term average deliveries. Idaho Power's briefing in IPC-E-04-08 and 10 is repeated here from MP28's responses to Idaho Power's claim for liquidated damages:[2]

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[2] Letter from Arkoosh Law Offices to Idaho Power, March 17, 2020, Exhibit F to the *Answer*.

The Commission Should Consider the Distinction Between Firm and Non-Firm QF Energy in Light of Current Conditions.

In seeking leave to file a post-hearing brief, counsel for U.S. Geothermal indicated that it was his intention to use the post-hearing brief to address the Commission's prior orders that define the terms 'none-firm' and 'firm' in the context of energy purchased from WFs. Idaho Power does not believe there is any dispute as to how the Commission has traditionally used those terms. In Order No. 15746 in Case No. P-300-12, The Commission noted that, 'under Section 292.304(d) of the FERC rules, a small power producer has the option of selling power to a utility either on an 'as-available' basis or 'pursuant' to a legally enforceable obligation.' In Order No. 15746 and subsequently in Order NO. 18190 issued in 1983 in Case No. *-1006-200, the Commission defined the 'as-available sale' to correspond to non-firm energy and the 'pursuant to a legally enforceable obligation' to correspond to firm energy. As the Commission noted in Order No. 18618 issued in Case No. U-1006-216, 'The Company is correct, therefore, when it asserts that Order Nos. 18190 and 18358 distinguish between firm and non-firm energy prices and that it is the 'quality of the energy produced' by the co-generator or small power producer that determines its price.' (Order No. 18618, p.3.)

In Order No. 18618, the Commission also stated:

"...energy is considered firm if it is provided by the seller pursuant to a legally enforceable obligation to deliver and if it is of sufficient reliability that it can serve to defer or avoid construction of the company's own plants. Hydro projects ---both those of the company and those of small power producers --- have always been assumed to meet this definition."
(Order No. 18618, p. 9).

As Idaho Power noted in its direct testimony in this case, using the definition of firm energy established in the early 1980's, a QF is only obligated to sign a contract and provide an estimate of what it thinks it will generate each month over the twenty (20) to thirty-five (35) year term of its agreement to be entitled to receive firm energy prices. As Mr. Gale noted, in today's world, the actual firmness of the energy deliveries under these 1980's vintage contracts more closely resemble non-firm energy deliveries than firm energy deliveries. In the Firm Energy Sales Agreements ('FESA's') without the 90%/110% band provision, QF developers provide an estimate of what they expect to generate each month, **but there is no requirement**, nor is there any economic incentive, for QF

> developers to provide accurate estimates or **to actually deliver energy in the monthly amounts they estimate they will provide in the Firm Energy Sales Agreement**. The actual amount of energy delivered by QF's under these agreements can fluctuate between 0 MW and 10MW, hour-to-hour, day-to-day, month-to-month, either because the project has lost its motive force or the developer has chosen to reduce generation for some other reason. With the exception of the five new QF contracts which include the 90%/110% band, Idaho Powers QF contracts do not require QF's to provide the higher value firm energy Idaho Power's customers are paying for.

Post-Hearing Brief, Page 4, Case Nos. IPC-E-04-08 and 10. [Emphasis added.]

The language of Idaho Power's Post Hearing Brief relevant to the operation of the Agreement deserves emphasis: There is no requirement...for QF developers to provide accurate estimates, or to actually deliver energy in the monthly amounts they estimate they will provide in the Firm Energy Sales Agreement.

2. Whether MP28 "permanently curtail[ed], in whole or in part its long-term average deliveries of the Annual Net Firm Energy Amount... ," by not producing for four months when Idaho Power acknowledged the repair period was neither a change in long-term average deliveries nor permanent.

The liquidated damage clause, Paragraph 21.3, activates only if "Seller permanently curtails in whole or in part its long-term average deliveries of the Annual Net Firm Energy [the estimate] specified in paragraph 6.3." Thus, at least three conditions must activate before the liquidated damage clause triggers.

First, the seller must permanently curtail deliveries of the estimated amount. Curtail means "cut-off." Webster's Seventh New Collegiate Dictionary. Permanently means "continuing or enduring without fundamental or marked change." Id. Permanent means continuing without marked change for the life of the Agreement. Did MP28 permanently cut-off estimated deliveries for the life of the Agreement?[3] Or, instead, has the estimate remained the same and actual deliveries of the estimate were reduced for only an interim of four months while the facility was repaired? Obviously the second event occurred. By the plain terms of the Agreement, MP28 did not permanently curtail.

Second, was the curtailment long-term? Again, the same answer obtains. As soon as the repairs were competed, the facility returned, as its operators intended it return, to deliveries of the estimated amount.

Finally, the obligation of the Seller in the Agreement is to seek to deliver an estimated amount of power, not a promise to deliver a fixed amount. The Agreement is deliberately structured to contemplate or anticipate delivery of an Annual Net Firm Energy (an estimate of 5,798,590 kWh) and not a commitment to deliver a particular Net Firm Energy amount (the actual delivery amount). This estimated amount of deliveries has not changed since 1994 and delivery is ongoing since conclusion of repairs in August 2019, just as Idaho Power knew it would be when it alleged an assessment of liquidated damages. Further, even though the Annual Net Firm Energy estimate was set at the execution of the contract, it remains a malleable aspiration throughout the contract because Idaho Power may change the estimate throughout the life of the contract. Paragraph 21.3 provides:

> The Annual Net Firm Energy amount in Article VI and the resulting Appendix D lump sum repayment amount may be adjusted from time to time based on the actual performance of the Facility.

[3] *Order No.* 21690, at page 11, spells out the computations resulting in Attachment D are: "For clarification, under IPCo's Appendix D methodology, the computed overpayment liability is the cumulative difference between the actual contract rate and what that rate would have been had it been computed by the same method for a shorter contract period." Stated another way, Appendix D penalties contemplate suspension of production under the contract for the remaining term. Suspension of production under the contract for the remaining term is thus what Paragraph 23.1 means as "permanent."

The parties clearly contemplated and understood that they could recalculate this target amount considering circumstances without fear of a penalty or reprisal if circumstances changed, unless there was a permanent (contract length) long-term curtailment by the operator. The fact that the Annual Net Firm Energy estimate can change according to circumstances enforces the interpretation that a seller is not penalized for deliveries under the estimate, but only for a long-term annual permanent curtailment, or permanent cut-off of the estimated amount.

When judging what circumstances the failure of plant production invokes Paragraph 21.3, the purpose of the clause must be given consideration. Initially, the Commission investigated an equitable means to protect ratepayers from overpayments to facilities caused by breach of levelized payment contracts when the contract provided a level payment during the life the contract. However, the avoided cost calculation assumed low energy prices early in the contract term and higher prices later in the term. Stated another way, the purpose of the provision is to protect ratepayers against a facility with a levelized price contract taking advantage of the lucrative early years and "walking away" later when the levelized contract price was less than the market price. See *Order No.* 26190. The two assumptions that caused the Commission in the first instance to investigate the need for security to protect ratepayers were, first, the assumption there would be high probability that a project owner receiving levelized payments will seriously consider 'walk-away;' then the late contract term payments would be a less than market value. *Id.* Neither of these concerns came to fruition with MP28. There was no 'walk-away,' but instead just a short repair period. Market prices are currently lower than the contract price providing ample incentive to push production, as well as proof that when Idaho Power went to the market and replaced the electricity not supplied by MP28 during the four months at issue, it made, or should have made, a better deal.

Interpreting Paragraph 21.3 against both the context in which it arose and in light of its purpose to protect ratepayers from late contract 'walk-aways,' the application of Paragraph 21.3 to the circumstances of this case is clearly inappropriate.

3. Whether liquidated damages are appropriate when the alleged harm is failure to deliver a product that trades in a fluid, granular, instantaneous market.

One can perceive from reading above that MP28 is not in breach of contract because MP28 has no obligation to deliver the estimated amount of power (Annual Net Firm Energy), only to deliver the power actually produced (Net Firm Energy). Paragraph 6.1 provides:

> 6.1 "Delivery and Acceptance of Net Firm Energy" - Except when either Party's performance is prevented by events of force majeure (Article XVI) or otherwise excused as provided herein, Idaho Power will purchase and Seller will sell all of the Net Firm Energy and Surplus Energy produced by the Facility and delivered by Seller to the Point of Delivery.

Notice the obligation is to deliver the Net Firm Energy (amount actually produced) and not the Annual Net Firm Energy (the amount estimated). MP28 delivered what it produced and is not in breach of contract. Thus, Idaho Power is not entitled to a damage claim of any kind.

Idaho Power argues entitlement to liquidated damages, however, this *Reply* will address the unenforceability of the liquidated damage clause in the contract, because the clause provides for a penalty, not damages.

A liquidated damage clause that amounts to a penalty cannot be enforced. A liquidated damage clause amounts to an unenforceable penalty when it is unreasonable compared to actual damages suffered. The Idaho Supreme Court has adopted a test to determine reasonableness.

The applicable principle is set out in 1 Restatement of the Law, Contracts, § 339, as follows:

> Liquidated Damages and Penalties.

> (1) An agreement, made in advance of breach, fixing the damages therefor, is not enforceable as a contract and does not affect the damages recoverable for the breach, unless
>
> (a) the amount so fixed is a reasonable forecast of just compensation for the harm that is caused by the breach, and
>
> (b) the harm that is caused by the breach is one that is incapable or very difficult of accurate estimation.

Graves v. Cupic, 75 Idaho 451, 456-57 (1954).[4]

Graves offers two other general binding observations. First, that the parties have agreed to a liquidated damage amount has no bearing. Secondly, if the effect of the clause is a penalty or the actual fair damage amount is not discernable, the courts deem the clause to be a penalty.

Paragraph 21.3 provides that a facility will pay Idaho Power liquidated damages in the event of permanent curtailment. Paragraph 21.3 provides for calculating an amount of liquidated damages by multiplying the relevant year multiplier found in Attachment D by the number of kWh Annual Net Energy Amount estimated less actual production after permanent curtailment. Idaho Power claims both permanent curtailments occurred and it is entitled to liquidated damages. The permanent curtailment issue is addressed above.

a. Whether the damages proposed are a reasonable forecast of just compensation for the harm alleged.

[4] Whether the validity of this liquidated damage clause is measured by Idaho's common law as set forth in *Graves*, or under the Idaho Uniform Commercial Code ("UCC") depends upon whether metered electricity is a "good" under the UCC. Idaho courts have not resolved this issue, and other courts are split. Whether the UCC or the common law cases control, however, does not appear to be of consequence because the tests of whether a liquidated damage clause is a penalty are nearly identical. Idaho Code §20-2-718 provides in pertinent part:

28-2-718. LIQUIDATION OR LIMITATION OF DAMAGES — DEPOSITS. (1) Damages for breach by either party may be liquidated in the agreement but only at an amount which is reasonable in the light of the anticipated or actual harm caused by the breach, the difficulties of proof of loss, and the inconvenience or nonfeasibility of otherwise obtaining an adequate remedy. A term fixing unreasonably large, liquidated damages is void as a penalty.

As pointed out by Idaho Power's answer in this matter, MP28 is paid more than straight line avoided cost in the early years and less than straight line avoided cost in the later years. When Paragraph 21.3 is applicable, it seeks a return to Idaho Power (not the ratepayer) of the amount paid over avoided cost for the remaining future years that were curtailed. Exhibit D displays the amount to be clawed back from the time of curtailment until the end of the contract period measured in dollars per annual MWh reduction resulting from the permanent curtailment. That amount increases each year from date of operation until year 24 when it begins to decline until the end of the contract. For year 25, the MP28 contract year in which the repairs were done, the claw back amount is $476 per annual MWh of permanent curtailment, that being applied to the difference between 5,798,590 kWh (estimated) and 3,355,049 kWh (produced) divided by 1000. The calculation was thus:

5,798,590 – 3,355,049 / 1000 X $476 = $1,163,429.[5]

Was this a reasonable contemplation of damage for the four months of lost production at the time of contraction in 1994? The clear answer is no.

Had MP28 met its estimate production for these four months, it would have produced 2,443,541 kWh additional electricity. Assuming an average contract price for this power of 48 mills/kWh, a reasonable forecast of loss in 1994 would have been $117,289.60. Because the avoided cost forecast in 1994 was determined at the time of forecasting to be the reasonable price of power in 2019 (although the seasonal avoided costs were averaged for this example), the reasonable cost of cover in 1994 would have been $117,289.60, not $1,163,429. Therefore, the claim for almost ten times what was the anticipated cost to cover the non-delivery is clearly a penalty.

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[5] Because the Agreement contains a partial forgiveness clause if the facility comes back online within three years, Idaho Power has considerably reduced its claim.

b. Whether the harm that is caused by the breach is one that is incapable or very difficult of accurate estimation.

Idaho Power must also show that during the MP28 25th contract year, it would be very difficult to determine the damage of not receiving the claimed electricity deficiency. This loss is measured by the market value of the energy at the time it should have been delivered.

In 2019, this Commission set avoided cost for non-levelized hydro-power under 10MW capacity at $26.64/MWh. The deficit claimed is 2,444 MWh, and thus the loss is $65,108.16.

Because Idaho Power is daily in purchases and sales of power, a calculation of the value of the loss of power it claims against MP28 is exceedingly ready at hand and easily performed, thereby disqualifying the use of a liquidated damage clause because it is no more than a penalty condemned by the Idaho courts.

V.

SUMMARY AND CONCLUSION

It must be remembered that the contractual obligation of MP28 under the Agreement is to produce the energy it produces unless it permanently cuts some or all of its production over the remaining term of the contract. Idaho Power unequivocally admits this in its briefing in Case Nos. IPC-E-04-08 and 10 when it asked the Commission to change this paradigm. Now, without explanation regarding what caused its change in position; without regard to the Agreement's language that the only obligation of MP28 is to deliver energy produced, not estimated; ignoring there has not been either a permanent or long term curtailment; and without perceiving what it desires in this case is an unenforceable penalty, not liquidated damages, Idaho Power is withholding money in breach of its Agreement with MP 28.

It is, therefore, respectfully requested that the Commission issue its determination consistent with this briefing that MP28 did not permanent curtail and that liquidated damages are not appropriate in the circumstances.

DATED this 17 day of September 2020.

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