BEFORE THE PUBLIC UTILITIES COMMISSION
STATE OF COLORADO

DOCKET NO. 02A-438E

IN THE MATTER OF THE APPLICATION OF PUBLIC SERVICE COMPANY OF COLORADO FOR APPROVAL OF LAMAR WIND ENERGY SUPPLY AGREEMENT AND FOR THE RATE MECHANISM TO RECOVER THE COSTS OF THE AGREEMENT

STIPULATION AND SETTLEMENT AGREEMENT

Public Service Company of Colorado ("Public Service" or "Company"), GE Wind Energy, LLC ("GE Wind"), the Staff of the Colorado Public Utilities Commission ("Staff"), the Colorado Office of Consumer Counsel ("OCC"), the Land and Water Fund of the Rockies ("LAW Fund"), and the Colorado Renewable Energy Society ("CRES") (all the foregoing entities referred to, collectively, as the "Parties"[1]) hereby enter into this Stipulation and Settlement Agreement (the "Stipulation").

INTRODUCTION

Public Service filed its application (the "Application") in this docket on August 21, 2002. The Application sought two things: first, approval by the Commission of a Wind Energy Supply Agreement ("WESA"), submitted with the Application, under which Public Service would purchase and GE Wind would sell electric energy from a proposed 162-megawatt wind farm (the "Project") to be constructed near Lamar, Colorado; and, second, a formal assurance by the Commission that, so long as it prudently administered the WESA, Public Service would be

[1] Holy Cross Energy is a party to this proceeding but has submitted a stipulation to the Commission indicating that it has intervened primarily to obtain copies of documents filed in this proceeding and that it will not actively participate in this proceeding. Consequently, this Stipulation is joined by all active parties to this docket.

entitled to recover from retail customers, through an adjustment clause to retail rates, 100% of all payments made under the WESA.

With the Application Public Service filed written testimony[2] and a Motion for Expedited Consideration. In response to the motion, the Commission assigned the Application to be heard on an expedited basis consistent with due process by Hon. Dale E. Isley, Administrative Law Judge.[3] The ALJ, in turn, conducted a pre-hearing conference (with all Parties except Holy Cross present), and set hearings in this matter for September 26 and 27, 2002.[4]

The Parties are now before the ALJ and the Commission seeking, in lieu of the scheduled contested hearing, forthwith approval, without any modification, of this Stipulation. The Stipulation is a negotiated settlement of all differences and disputes among the Parties on issues raised by or related to the Application. Part of the Stipulation will require Public Service and GE Wind to enter into a new amendment to the WESA (hereafter, the "Amendment"), to be explained below. The Stipulation calls on the Commission to grant expedited approval of (A) the WESA as filed, and as modified by the Amendment; and (B) full recovery by Public Service of all prudently-incurred expenses incurred under the WESA, as thus amended, with recovery coming initially from retail customers, but requiring Public Service to take certain steps to attempt to recover the wholesale jurisdictional portion of those payments from its wholesale

[2] The Parties ask that this testimony and all public comments be admitted as part of the official record for this docket and that it be available for reference as the ALJ and the Commission consider this Stipulation. *See* testimony of Public Service witness Gary A. Swarts, to which the WESA was attached as an exhibit; testimony of Public Service witness James F. Hill; and testimony of GE Wind witness Robert H. Gates.

[3] *See* Decision No. C02-1005 (September 10, 2002).

[4] By Decision No. R02-1023-I (September 13, 2002), the ALJ scheduled a pre-hearing conference in this matter for September 18, 2002. Following the pre-hearing conference on that date, the ALJ issued Decision No. R02-1035-I (September 19, 2002), which granted the requests to intervene of LAW Fund, CRES, Holy Cross and GE Wind; accepted a stipulation between Public Service and Holy Cross regarding the scope of Holy Cross participation; set hearings in this matter for September 26 and 27, 2002; and established procedures for pre-hearing discovery and filing of answer and rebuttal testimony.

customers. Finally, the Stipulation provides that, immediately on receipt of all the foregoing Commission approvals, Public Service and GE Wind will execute the WESA, which has not yet been signed, as well as the Amendment.

While no testimony other than that pre-filed by Public Service with the Application has been submitted in this docket, the Parties acknowledge that, were a contested hearing to be held, both Staff and the OCC would present evidence and testimony opposing certain provisions of the WESA as filed, and/or certain aspects of the Company's request in the Application for full recovery from retail customers of payments to GE Wind under the WESA. The LAW Fund and CRES would have presented testimony on the benefits of the Project. The Parties acknowledge that they have either participated in or been apprised of the substance of numerous discussions in which Staff, the OCC, CRES, and the LAW Fund have communicated the bases for their positions. Through a process of informal discovery, Staff, OCC, LAW Fund, CRES, and GE Wind have been provided by Public Service with various documents, and answers and explanations for various concerns and questions. The Parties represent that as a result of their discussions and of the exchange of documents and information that has occurred, they are able at this point to compromise positions they have asserted or would assert in this docket and reach a settlement.

THE DISPUTED ISSUES

Section 6.1 of the WESA. The principal issue of contention among the Parties has concerned section 6.1 of the WESA. Section 6.1 provides that if Public Service is unable to accept delivery of energy from the Project because of a transmission constraint that the Company can alleviate by "backing down" non-wind electric generation that the Company controls, Public Service will "back down" the non-wind generation in order to take all of the Project's wind

production[5]; or, if it does not, will nevertheless pay the Project for all energy the latter could have delivered at the time.

While the parties do not object to the inclusion of section 6.1 in the WESA, there is disagreement about the allocation of risk for payments made because of transmission constraints. The Parties' positions will be discussed in more detail, below.

Public Service Cost Recovery. The second issue of principal contention relates to the Company's request in the Application for full cost recovery from retail ratepayers of all payments for wind energy under the WESA. The Parties disagree about whether retail customers should pay for all the wind energy or whether this expense should be shared with the Company's wholesale customers. Their positions on these issues will also be discussed in more detail below.

DISCUSSION OF THE DISPUTED ISSUES

Section 6.1 of the WESA. The provision was intended by Public Service and GE Wind to address a potential temporary limitation on the Public Service transmission system to the south of Denver, specifically between Midway, which is south of Colorado Springs, and the southern suburbs of Denver.[6] The potential limitation is the result of the possibility that the power lines that connect Midway and south Denver at the present time lack the capacity, at certain peak usage times, simultaneously to transmit all of the power available from both the Project and from other power plants Public Service controls south of Denver.

[5] Section 6.1 only applies to limitations of transfer capacity that Public Service can address by backing down generators other than the Project. Thus, it does not apply to certain power line outages. For example, if the power line to which the Project is directly interconnected at Lamar went down, no power at all could flow northward from that point. This would not be a situation Public Service could address by re-dispatching other power plants. The Project might simply have to forgo payment until the line was repaired.

[6] The transmission path discussed is sometimes referred to as one between Midway and Daniels Park, and sometimes as one between Midway and Smoky Hill. Both Daniels Park and Smoky Hill are substations in the southern Denver suburbs. To alleviate the potential transmission path constraint being discussed, Public Service originally intended to build a new line between Midway and Daniels Park. In fact, the current plan is for the new line to run from Midway to Smoky Hill.

Public Service plans to seek approvals for a new transmission line, from Midway to Smoky Hill, that would alleviate transmission constraints between Midway and the Denver area. In addition to seeking approvals and permits from the affected parties,[7] the Commission has required Public Service to apply to the Commission for a Certificate of Public Convenience and Necessity (CPCN). The current anticipated in-service date for the new transmission line is October 31, 2005. However, there is no guarantee that Public Service will be successful in obtaining all the permits necessary to build this line or that the CPCN and other permits will be granted in time to meet the projected October 2005 in-service date.

The Project is scheduled to be in commercial operation at the end of 2003. Thus, the potential constraint being discussed could affect energy deliveries from the Project for no more than two years, if Public Service is able to obtain a CPCN from the Commission and all required local land use permits on a timely basis and there are no other impediments to timely construction.

Public Service and GE Wind take the position that section 6.1 is consistent with the fact that the WESA, like many contracts for wind power, is a "delivery contract." Unlike other third-party power providers from whom Public Service purchases, the Project does not receive monthly capacity payments simply for being "on call," or available, to generate. The Project receives payment for the energy it delivers, exclusively. If the wind does not blow, and the Project cannot produce energy, it does not get paid. If the wind does blow, and it can produce energy, the Project desires to be paid for its energy.

GE Wind insisted on section 6.1 when it learned of the potential constraint on the Company's transmission system south of Denver, because of the financial reality that the Project

[7] Affected parties potentially include the counties of Arapahoe, Elbert, El Paso, and Lincoln, as well as the City of Aurora.

is paid only for deliveries, not for being "available" to deliver. Financing the Project could be impeded or made significantly more expensive if there were an open-ended possibility that the Project would be curtailed, even when the wind was blowing, because the transmission path northward from the Project was restricted. GE Wind therefore insisted that, at times when transfer capacity on the northward path is limited, where Public Service has other generation facilities it could back down or re-dispatch, that other Public Service generators should be curtailed. In recognition of the nature of wind energy supply contracts, its ability to re-dispatch other generation to relieve the expected constraint, and the project finance realities faced by GE Wind, Public Service agreed.

Public Service and GE Wind also take the position in this docket that section 6.1 is a reasonable response to the exigencies of the transmission path constraint south of Denver because the Commission was made aware of the constraint at the time the Commission required Public Service to enter into a purchase agreement with GE Wind's predecessor in interest, Enron Wind Development Corp. ("Enron Wind"). Enron Wind, it will be recalled, bid the Project into the supply-side solicitation component of the Company's 1999 Integrated Resource Planning process. Public Service declined to select the Project as a winning bid. The Commission ordered the Company, over its objections, to accept the project and proceed to contract negotiation. *See* Decision No. C01-295 (March 28, 2002) (hereafter, "1999 IRP Decision") in Docket No. 99A-549E—Phase II. In that decision, the Commission addressed the potential transmission constraint as follows:

> We conclude that potential transmission infrastructure impacts of the Lamar facility [the Project] should be given minimal weight in our decision. The Company introduced this concern in its rebuttal testimony. At the hearing, witness Eves testified that the Company's concerns regarding transmission constraints are focused on the two-year period 2003-2004, and for the area south

> of Denver from Midway to Daniels Park. Those constraints will be relieved beginning in 2005 once the Midway-Daniels Park transmission project is completed. Thus, the Company's concerns are effectively limited to a two-year period during the fifteen-year life of the proposed Lamar [Project] contract. Even for this two-year period, the evidence provided by the Company does not give us a good basis for determining the actual likelihood of a transmission constraint occurring.

1999 IRP Decision at page 43.

Staff and the OCC take the position that this language from the 1999 IRP Decision is no more than Commission recognition that Public Service expressed concern about the Midway-Denver transmission path. Staff and the OCC dispute that this language indicates the Commission in any way found Public Service's concern to be valid. Staff and the OCC also point out that this language does not in any way authorize Public Service and the Project to enter into a provision similar to section 6.1 of the WESA. Therefore, Staff and the OCC believe that Public Service should bear the risk of any additional cost of backing down lower-cost generation in order to accept wind energy, when that backing down is due to transmission constraints. Furthermore, Staff and the OCC believe that, prior to and subsequent to bringing potential transmission constraints to the Commission's attention in its 1999 IRP docket, there were steps that Public Service should have taken that, if taken, would have reduced or eliminated potential transmission constraints.

Staff and the OCC have raised the concern that it is possible that power from the non-wind generators that are curtailed under section 6.1 of the WESA due to transmission constraints, in order for Public Service to accept deliveries from the Project at peak times, may be less expensive than energy from the Project. Staff, the OCC, and the LAW Fund asked Public Service to estimate the number of hours in the years 2003, 2004 and 2005 that accepting energy deliveries from the Project might require Public Service to curtail non-wind generation sharing

the transmission path into Denver from the south. Staff, the OCC, and the LAW Fund asked that the cost of power from the curtailed non-wind generators be compared to the price paid by Public Service to the Project for wind-generated energy.

In response to these requests, Public Service prepared a confidential hourly analysis of the type requested for all 8,760 hours of each of three years—2003, 2004 and 2005. The Parties have reviewed and discussed this analysis at length. It shows that the hours during which non-wind Public Service-controlled generation would be likely to be curtailed are very few; and that the cost differential in those hours between Project energy actually delivered and non-wind generation "backed down" is on the order of a few tens of thousands of dollars, total, over the three years in question. However, both Public Service and the other Parties recognize that this analysis was not a sophisticated computerized modeling analysis and was, at best, a simplified spread-sheet analysis. In addition, all Parties recognize that the conclusions reached by the simplified spread-sheet analysis may be flawed because of the large number of unknown variables that must be assumed in order to perform the bottom-line calculations. Therefore, while the Parties have found this analysis useful to develop this Stipulation and Settlement, the Parties have agreed that the analysis should not be submitted to the Commission as part of this Stipulation.

All Parties agree that the Commission has determined that the Project produces system benefits. The pre-filed testimony of Public Service witness James F. Hill in this docket contains two economic analyses of the WESA. The first analysis compares the original Enron Wind bid terms with the terms of the WESA using the same PROSCREEN II modeling assumptions that

were used to evaluate the Enron Wind bid in the Company's January, 2001, final IRP filing.[8] This analysis shows that the WESA provides $1.1 million (NPV 1999) more savings than would have been provided by the original Enron Wind bid. These additional savings constitute approximately 0.8% of the payments under the WESA; Mr. Hill concludes that the WESA and the original Enron Wind bid are economically equivalent.

Mr. Hill also performs a second economic analysis in PROSCREEN II using updated modeling assumptions as of June, 2002, to determine whether the WESA is still an economic purchase for Public Service. In this analysis Mr. Hill also uses the LAW Fund assumptions of ancillary costs, and Mr. Hill includes $1.892 million in interconnection costs that were not considered in the bid evaluation presented to the Commission in Public Service's 1999 IRP. Mr. Hill concludes that using June, 2002, PROSCREEN modeling assumptions, and including interconnection costs, the Project will result in savings of $6,898,000 (1999 NPV). He concludes that passage of time during contract negotiations has not diminished the value of the WESA.

Staff and the OCC take the position that it would not be appropriate to include in rate base interconnection costs that were not modeled and presented to the Commission for its approval during Public Service's 1999 IRP.[9] This position is based upon the belief of Staff and the OCC that the original bid analysis should form the basis of any contractual agreement entered into by the Company. Adding costs at a later date undermines the net positive benefit to ratepayers and compromises the integrity of the IRP process.

Public Service takes the position that the interconnection costs included in Mr. Hill's analysis are properly included in the Company's cost of service and are recoverable from

[8] There is one exception. Mr. Hill's analysis uses the ancillary service costs associated with the Project that were sponsored by the LAW Fund in Public Service's 1999 IRP docket, *supra*. This is consistent with the Commission's directive in the 1999 IRP Decision.

[9] Because of the expedited nature of this procedure, Staff did not conduct an independent verification of Mr. Hill's analyses.

ratepayers. Public Service explains that the GE Wind interconnection costs were not modeled in the Company's 1999 IRP Report because the Company had not recommended the GE Wind project as part of its preferred portfolio.

The LAW Fund takes the position that approval of the WESA will provide significant economic benefits to ratepayers, as illustrated by the Commission's 1999 IRP Decision. In addition, the LAW Fund asserts that the Project will create additional benefits, including fuel diversity benefits, environmental benefits, and rural economic development benefits for southeastern Colorado. The LAW Fund's position is that the potential cost to ratepayers of the transmission constraint are minor compared to the sizeable economic and environmental benefits. The LAW Fund concurs with the OCC and Staff that there are steps that Public Service could have explored that may have reduced potential transmission constraints.

CRES is in support of the Staff, OCC, and LAW Fund positions.

Despite Mr. Hill's analyses, the Parties recognize that the operation of section 6.1 could still result in some costs from re-dispatch of Public Service-controlled non-wind generation that would have supplied energy at a lower price than the Project. The approach the Parties have adopted to compromise their positions is set forth after the immediately following discussion of the "full recovery" issue.

Public Service Cost Recovery. In its 1999 IRP docket, Public Service argued that, if it were required against its will to enter into a purchase agreement with the Project, it should also be entitled to full recovery of all payments for Project energy. The Commission responded as follows:

> We agree with the Company that it should be granted an opportunity to recover all the costs associated with power purchase from Lamar [the Project], especially since this purchase is pursuant to our directive in this decision. However, there is no need for us

> to specify the cost recovery mechanism here. This decision directs the Company to attempt to acquire the Lamar facility as part of its 1999 IRP. We now confirm that PSCo is entitled to an opportunity to recover the costs associated with any power purchases from Lamar.

1999 IRP Decision at page 44.

Public Service takes the position that in order to have an opportunity to fully recover the costs associated with any power purchases from the Project, Public Service needs confirmation from the Commission that it may pass on 100% of its prudently-incurred expenses under the WESA to retail customers through an automatic adjustment clause. Public Service argues that payments under the WESA are not in the test year under consideration in Public Service's pending rate case and therefore will not be reflected in base rates. Public Service further maintains that it cannot recover any portion of these payments from its wholesale customers under Public Service's current wholesale rates. Consequently, in order to have an opportunity for full cost recovery, as promised by the 1999 IRP Decision, Public Service has requested in its application that 100% of the WESA expenses be recovered from retail customers through an adjustment clause to retail base rates.

Staff and the OCC object to an open-ended recovery of all the WESA expenses from retail customers. Staff and the OCC maintain that wholesale customers should pay their allocated share of these expenses. Further, Staff and the OCC argue that Public Service should not be given a blank check for all payments under the WESA. Staff and the OCC maintain that Public Service is still required to administer the WESA and to otherwise conduct its business in a prudent manner and to be subject to cost disallowance if the Company fails to act prudently.

SETTLEMENT OF DISPUTED ISSUES

After significant hours of discussion and negotiation, the Parties have reached full settlement of all disputes that have arisen or could arise among them in this Docket. The Parties hereby stipulate as follows with respect to the Company's Application in this Docket:

1. To mitigate potential adverse impacts on ratepayers due to constrained transmission during the first two Commercial Operation Years (as defined in the WESA), GE Wind has offered to reduce the payments to which it would otherwise be entitled under the WESA, by an amount that the Parties agree is substantially higher than Public Service's simplified spread sheet estimate of the likely cost to ratepayers caused by the re-dispatch of southeastern Colorado generation to accept the wind energy due to the current insufficient transfer capability between Midway and Denver. GE Wind has agreed to accept a reduced Contract Energy Payment Rate (as defined in the WESA) for the first two Commercial Operation Years, and only for the first two Commercial Operation Years, such that the rate otherwise payable is reduced by $0.10 per megawatt-hour ("mWh"). Over the two years the Contract Energy Payment Rate reduction is in effect, given the estimated average facility annual production of 534,000 mWh, GE Wind would receive approximately $106,000 less than it would have been paid without this stipulated reduction, depending on wind and other conditions. To accomplish this payment reduction, the WESA as filed with the Commission would remain unchanged, except that GE Wind and Public Service, upon approval of this Stipulation, agree to enter into an Amendment to the WESA to reflect this two year reduction in the Contract Energy Payment rate.

2. The Parties agree that the reduced Contract Energy Payment rate will be accepted as "liquidated damages" to mitigate potential costs to Public Service and its ratepayers caused by

the re-dispatch of generation under Article 6.1 of the WESA, during the first two Commercial Operation Years under the WESA. With the Amendment to the WESA required by paragraph 1, the Parties withdraw all objections to the WESA and support Commission approval of the WESA, as amended.

3. All Parties withdraw their objections to the Company's recovery of the interconnection costs of the GE Wind Project.

4. In its Application, Public Service seeks 1) Commission approval of the WESA and 2) recovery from retail customers through an automatic adjustment clause of all prudently-incurred expenses under the WESA. By entering into this Stipulation, no party is waiving its right to contest in a future Commission proceeding the prudence of any action taken by Public Service, other than the actions specifically contemplated by this Stipulation. The actions specifically contemplated by this Stipulation are:

a. Public Service will sign and be bound by the WESA and the Amendment required by this Stipulation.

b. The two year reduction in Contract Energy Payment Rate set forth in the Amendment will serve as a "liquidated damage" remedy to mitigate prudently incurred increased expenses (if any) passed through to retail ratepayers under the WESA due to re-dispatch of facilities during the first two Commercial Operation Years of the Project.

c. Public Service is entitled to fully recover its prudently-incurred expenses under the WESA through an automatic adjustment clause on retail rates, but Public Service must seek recovery of a portion of these expenses from Public Service's wholesale customers in accord with paragraph 4, below.

5. Public Service shall be entitled to recover from retail customers 100% of its prudently-incurred expenses under the WESA until such time as Public Service obtains approval from the Federal Energy Regulatory Commission ("FERC") to include recovery of a portion of the WESA expenses in Public Service's wholesale rates (either base rates or an appropriate adjustment clause). Public Service agrees to apply to FERC for such approval no later than six months after the Commission's final order with respect to Public Service's Air Quality Improvement Rider, pending before the Commission in Docket No. 02S-485E. Public Service further agrees to make a diligent, good faith effort to persuade FERC to approve recovery of WESA expenses from Public Service's wholesale customers. If Public Service fails to make such timely application to the FERC or to expend such diligent, good faith effort, then the portion of WESA expenses that would have been recoverable from wholesale customers shall no longer be recoverable from retail customers. All revenues that Public Service receives from its wholesale customers for WESA expenses shall be credited as an offset to the retail adjustment clause recovering the WESA expenses.

6. Public Service and GE Wind agree to execute the WESA and the Amendment contemplated by this Stipulation immediately upon Commission approval of this Stipulation.

7. All parties support expedited approval by the Commission of the Company's Application, as amended by this Stipulation, with the objective of obtaining such approval by October 1, 2002, or as soon thereafter as possible.

8. All parties hereby stipulate that any objections they might have had to the WESA or Public Service's Application, as modified by this Stipulation, are withdrawn and that they support this Stipulation and Settlement Agreement as being in the public interest.

REQUEST FOR COMMISSION APPROVAL

The Parties agree that this Stipulation and Settlement Agreement shall be filed as soon as possible with the Commission for Commission approval. This Stipulation and Settlement Agreement shall not become effective until the issuance of a final Commission order approving the Stipulation and Settlement Agreement, which order does not contain any modification of the terms and conditions of this Stipulation and Settlement Agreement which is unacceptable to any of the Parties. In the event the Commission modifies this Stipulation and Settlement Agreement in a manner unacceptable to any Party, that Party shall have the right to withdraw from this Agreement and proceed to hearing on some or all of the issues that may be appropriately raised by that Party in this docket. The withdrawing Party shall notify the Commission and the Parties to this Agreement by e-mail within one business day of the Commission modification that the Party is withdrawing from this Agreement and that the Party is ready to proceed to hearing; the e-mail notice shall designate the precise issue or issues on which the Party desires to proceed to hearing (the "Hearing Notice"). The withdrawing Party shall file with the Commission a formal notice, containing the same information as the e-mail Hearing Notice on the same day that the withdrawing Party sends the e-mail Hearing Notice. The withdrawal of a Party shall not automatically terminate this Agreement as to any other Party, but any other Party may also withdraw upon receiving another Party's Hearing Notice by serving the Commission and the other Parties with its own Hearing Notice by e-mail within one business day of the date of the Hearing Notice from the first withdrawing Party. A Party who properly serves a Hearing Notice shall have and be entitled to exercise all rights the Party would have had in the absence of the Party agreeing to this Stipulation and Settlement Agreement. Hearing shall be scheduled on the issues designated in the Hearing Notices of the withdrawing Parties as soon as practicable.

The negotiations or discussions undertaken in conjunction with the Stipulation and Settlement Agreement shall not be admissible into evidence in this or any other proceeding, except as may be necessary in any proceeding to enforce this Stipulation and Settlement Agreement.

Approval by the Commission of this Agreement shall constitute a determination that the Agreement represents a just, equitable and reasonable resolution of all issues that were or could have been contested among the Parties in this proceeding.

The Parties to this Agreement state that reaching agreement in this docket as set forth in this Agreement by means of a negotiated settlement is in the public interest and that the results of the compromises and settlements reflected by this Agreement are just, reasonable and in the public interest.

Except as otherwise specifically agreed in this Agreement, nothing contained herein shall be deemed as constituting a settled practice or legal precedent for the purposes of any other proceeding that does not involve this Stipulation and Settlement Agreement.

This Agreement may be executed in counterparts, all of which when taken together shall constitute the entire Agreement with respect to the issues addressed by this Agreement.

DATED this 26th day of September, 2002.