Buying Back the Dams: An Important Billion Dollar Decision for Montana

When NorthWestern Energy announced last year that it had entered into an agreement to buy back the hydroelectric facilities that the Montana Power Company once owned, most Montana’s probably smiled a little, thinking that a serious public policy mistake of the 1990s was about to be corrected.

Those hydroelectric facilities had been the backbone of the Montana electric system since early in the twentieth century and the source of Montana’s low cost electricity. Montana Power sold the hydroelectric dams off in a frenzy of fantasy in 1999 as it tried to get out of the newly deregulated electric power industry and become purely a telecommunication company. Within a couple of years, Montana Power in its new corporate form, Touch America, was bankrupt and the hydroelectric generators were owned by a Pennsylvania utility, Pennsylvania Power and Light, which had gone the opposite direction in response to electric utility deregulation, buying up as many electric generating facilities as possible, no matter how far they were from PPL’s home in eastern Pennsylvania.

Montana Power’s sale of all of its generating assets to an out-of-state corporation left Montana Power’s old customers entirely dependent on electricity purchased on the Pacific Northwest’s regional electric markets at whatever the price happened to be. The new utility that owned the wires that continued to deliver the electricity to Montana households and businesses, NorthWestern Energy, had no generating resources of its own to meet its customer’s needs. When electric prices in the Pacific Northwest
electricity market were low, this was a good deal. When, as in most years between 2000
and 2010, market electric prices were high, that was not so good. Both household and
business budgets were regularly disrupted by spikes in the cost of purchasing
electricity.

So getting those hydroelectric dams back and finishing the rebuilding of
NorthWestern Energy’s portfolio of electricity resources may well have encouraged
smiles from customers.

But there was a not so small offsetting consideration: The price tag: almost a
billion dollars, $900 million, to be exact.

Imposing a financial obligation that high on Montana electric customers was
bound to raise eyebrows and furrow brows. Part of this “sticker shock” is tied to the
difference between a monthly rental payment and the cost of buying outright ownership.
Monthly rent on a house is likely to be measured in hundreds of dollars while
purchasing the house may be measured in hundreds of thousands of dollars. But most
of us still choose to buy a home.

We all regularly have to compare costs spread over time to lump-sum investment
costs. We do it when we buy cars and homes or any time we buy something on credit.
Fortunately there are analytical tools available to help investors and consumers make
such decisions.

But there are also aspects of such decisions that are harder to quantify and then
weigh. Some of them have to do with uncertainty and risk. If NorthWestern were to
remain primarily an electricity buyer for us in the regional electric markets, we do not
really know what that electricity will cost in the future, just as you might not know what
your rent would be five or ten years from now if you did not buy a house. Also, there are alternative ways to get electricity other than buying the hydroelectric plants. NorthWestern could build a natural gas fueled plant or buy ownership in some existing coal-fired generator. But then the future cost of operating those plants would be unknown. Natural gas prices have fluctuated widely over the last decade or so and the costs of environmental controls on coal-fired plants have been rising steadily. Just as purchasing a house usually fixes your monthly payments off into the future, buying the hydroelectric plants that have no fuel costs largely freezes the costs of that electricity at current levels on into the future and removes a significant part of the uncertainty about future electricity costs.

These are familiar types of risk against which consumers and investors regularly try to protect themselves by “hedging” against future price fluctuations in one way or another. That, like all insurance policies, costs something, but one can always ask the subjective question of whether the cost of that protection or insurance is worth the reduction in risk.

But as with any business or investment decision, there are other aspects of the purchase of the Montana hydroelectric plants that are important and also have to be subjectively evaluated. These include the desire to “repatriate” the dams by having the electric utility that serves much of Montana control those electric assets subject to the oversight of an elected Montana Public Service Commission.

Montanan’s built those dams and have operated and paid for them for over a century. The Montana electricity transmission and distribution systems were designed around them. The dams occupy our major rivers providing a large supply of renewable
and sustainable electric energy. They are here in our backyard, standing ready to serve
our electricity needs, not located at some unknown place thousands of miles away.
That hydroelectric generation flows not from a single huge plant but from 11 different
facilities each of which, in turn, has multiple generators being turned by the falling water.
They are also located across varied parts of Montana's geography so that they are not
tied to just one local micro-climate.

Clearly there are a lot of positive features associated with these hydroelectric
generators being dedicated, once again, to serving Montanans' needs. But then again,
$900 million is a lot of dollars. It will be the Montana Public Service Commission’s job to
weigh both the advantages associated with once again regaining the control and use of
these valuable energy resources as well as the price tag associated with buying them
back.

This clearly is one of the more important decisions that the Montana Commission
has ever been asked to make.