Dealing with a “Speculative and Uncertain” Future When Planning Electric Supply Acquisitions

Three decades ago, Montana was tangled up in a debate over how to meet our future electric needs. The Montana Power Company had two large electric generators under construction at Colstrip, Colstrip Units 3 and 4. Most of that new generation was headed to west coast utilities, but Montana Power had a 30 percent interest in both of those generators. The debate was over the environmental impacts of the huge new generators, their cost to customers, and whether Montana customers actually needed all that power.

Initially the Montana Public Service Commission ruled that Montana customers should not be responsible for the costs associated with either of those new electric generators. After much political and legal tussling, Montana Power agreed not to ask customers to pay for Colstrip 4 and the Montana Public Service Commission agreed to have customers pay for Montana Power’s share of Colstrip 3. Given the huge investment that Montana Power had made in those new generators, the power company faced potential bankruptcy if it could not find a customer for that power and produce a cash flow to pay for its share of the generator. It was a traumatic period for customers, regulators, and Montana Power stockholders.

Partly to avoid a repeat of the Colstrip fiasco, Montana Power, the Montana Public Service Commission, and the state legislature agreed to an electric utility planning process that would require power companies to carefully analyze the future demand for electricity, the alternative ways of meeting that future demand, and the risks
and costs, including market, environmental, and regulatory risks and costs, of the alternative sources of supply.

The process now underway before the Montana Public Service Commission, analyzing NorthWestern Energy’s proposal to buy back the hydroelectric generators once owned by the Montana Power Company, involves the same sort of analysis of electric supply alternatives that was put in place a quarter-century ago.

NorthWestern Energy thinks that buying back the hydroelectric projects will help reduce future risks significantly, but at an up-front cost. NorthWestern likens that up-front cost to the cost of an insurance policy that protects you against potential future losses. The critics of the hydro re-purchase, on the other hand, say that NorthWestern is asking customers to pay higher electric prices now based on “speculative and uncertain” future events that may never occur. As a result, they say, customers will be burdened on into the future even if those feared future events never take place.

Conceptually, it is difficult to understand that criticism. That logic would suggest that none of us should ever buy, say, fire insurance. Almost none of us will see our homes burn down. Yet most of us make fire insurance payments year-in and year-out. Obviously we pay attention to the cost of that insurance, but we do not dismiss the idea of paying some insurance costs just because a future house fire is “speculative and uncertain.” If such events were not “speculative and uncertain,” we would know exactly what was going to happen and when, and we would take steps to avoid that damage.

It is the politically loaded character of one of the major risks associated with coal and natural gas fueled electric generation that actually energizes the critics of the hydroelectric buy-back: namely the risk and costs of government regulations aimed at
reducing carbon emissions from fossil-fuel-burning electric generators. But one can be opposed to possible negative consequences and still take steps to minimize the risk of them damaging us. None of us want our home to burn down, and we take steps to keep that from happening, but we still have fire insurance.

The regulation of carbon emissions is not really “speculative and uncertain.” EPA regulations of the carbon emissions from new electric generators will be publish in four months. The EPA regulations for carbon emissions from existing electric generators will be published in about a year and states will then have another year to develop their implementation plans. Dozens of older coal-fired electric generators are being retired nationwide including the only coal-fired generators in Washington and Oregon. Regulation of carbon emissions is underway. The costs are beginning to be felt. It would be foolhardy for NorthWestern Energy to ignore that fact when choosing additional electrical resources to fill out the electric supply portfolio that serves its Montana customers.

NorthWestern Energy is mandated by good business sense as well as state law and Montana Public Service Commission regulations to face uncertainty directly and mitigate the costs associated with it, not ignore it because it is “uncertain.” That includes the uncertain cost of carbon regulation, the uncertain regional electric market prices, the uncertain natural gas and coal prices, the uncertain water flow in our rivers, the uncertain demand of its customers, the uncertain weather, etc. etc.

NorthWestern claims to have done that and concluded that re-purchasing the Montana Power hydroelectric resources will help significantly in managing many of those risks. We should be focused on that NorthWestern risk management strategy that
seeks to cope with an unavoidably uncertain future and the costs and benefits associated with that strategy. It was for good historical reasons that electric utility planning in Montana and elsewhere set aside the childish fantasy that we live in a certain and predictable world.