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8 **BEFORE THE GUAM PUBLIC UTILITIES COMMISSION**

9 IN THE MATTER OF:)
10)

11 GUAM POWER AUTHORITY)

12 LEVELIZED ENERGY ADJUSTMENT)

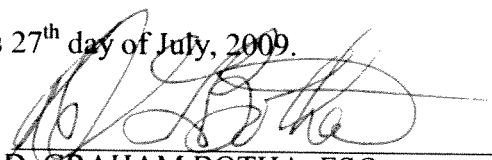
13 CLAUSE (LEAC))

DOCKET NO. 02-04

**GPA RESPONSE TO GCG REPORT ON
LEAC FILING**

14 **COMES NOW**, the GUAM POWER AUTHORITY (GPA), by and through its counsel
15 of record, D. GRAHAM BOTHA, ESQ., and hereby files its response to the Georgetown
16 Consulting Group (GCG) Report dated July 21, 2009.

17 **RESPECTFULLY SUBMITTED** this 27th day of July, 2009.

18 
19 **D. GRAHAM BOTHA, ESQ.**
20 **GPA Legal Counsel**



GUAM POWER AUTHORITY

ATURIDÁT ILEKTRESEDÁT GUAHAN
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July 24, 2009

Mr. Frederick J. Horecky
Legal Counsel
Public Utilities Commission
643 Chalan San Antonio, Suite 102B
Tamuning, Guam 96913

RE: August 1, 2009 Levelized Energy Adjustment Clause Factor

Dear Mr. Horecky:

The Guam Power Authority (GPA) has reviewed the Georgetown Consulting Group (GCG) report on LEAC dated July 21, 2009 and we wish to provide you our comments.

The fuel markets have been exceedingly volatile in the last few months. The Authority received approval to petition for a change in the Levelized Energy Adjustment Clause (LEAC) factor in May of this year. For a few weeks after the authorization was received, fuel prices moved in an upward direction. After that, prices began to pull back for a couple of weeks. This pattern has continued to this day. This has made predicting future fuel costs very challenging. Adding to the difficulty is the fact that two of GPA's hedge providers are expecting some downward pressure in the market over the next six months.

GPA has discussed internally whether or not an updated filing should be made, however, with all the mixed signals being sent by the market, the Authority has been unable to forecast a better price than that included in the filing. GPA agrees with GCG that the price from July 7 utilized in their report is most likely a better representation of where fuel costs will be in the future.

The GCG report also indicates they corrected a logic error on the part of GPA. The subject has to do with the carrying cost associated with fuel inventory maintained by the Authority. When the price of fuel increases, the Authority must tie up more cash in fuel inventory costs even though the volume stays the same. The increasing fuel costs in recent years have had a negative impact on the Authority. When prices increase, GPA is forced to make up for the use of cash by transferring from its Working Capital Fund, decreasing the levels of materials inventory, and deferring capital improvement expenditures.

From 2005 to 2007 the carrying cost of GPA's inventory increased by approximately \$16 million. GPA was forced to absorb these increased costs. The Working Capital Fund was virtually empty, GPA's materials inventory was at its lowest level in a decade and capital projects were severely cut back. During this period, GPA raised the issue at a status conference of whether inventory cost changes could be rolled into the LEAC. At the time, GCG advised that it would not be an appropriate regulatory practice to place such fuel adjustments in the LEAC, but they should be dealt with as part of a base rate case. As a result of this situation, GPA included a \$5.3 million annual cost adjustment factor in its rate petition filed in the fall of 2007. During the rate proceedings, GCG determined that rather than building a \$5.3 million cost increase into the revenue requirement, it would be better to include the amount into the LEAC. However, they recommended that implementation of the adjustment to be effective in 8/1/08. The next LEAC rate went into effect in October 2008 and included an adjustment for the carrying cost of fuel in the total amount of \$23 million – the actual increase in carrying cost from 10/1/07 when inventory was priced at \$64/bbl to its estimated carrying cost \$115.36/bbl at 10/1/08. The PUC order authorizing this recovery went into effect on 10/3/08. However, before GPA had an opportunity to recover these funds that had been tied up in inventory costs, the price of fuel had already begun to fall and the decrease in inventory carrying costs was creating a liability for the Authority.

In the February 1 LEAC filing, GPA petitioned the PUC to have its fuel inventory adjustment be capped at \$64.46/bbl. In other words, GPA had been authorized to recover the difference in fuel costs from \$64.46 to \$115.36, therefore, as prices fall, GPA should only be required to return the difference between \$115.36 to \$64.46. The position was rejected by GCG. The GCG position was that even though GPA had been forced to absorb the burden of the increased fuel inventory carrying value, up to \$64.46/bbl, it should further be harmed by absorbing the payment to ratepayers for the cost of fuel dropping below \$64.46. During the January 2009 status conference, GCG relented from their position and agreed to a one time reprieve from the prior PUC order wherein all inventory fluctuations would be recovered from or paid out through the LEAC. It was GPA's understanding that after the one period reprieve, GPA would be entitled to all future fuel inventory cost movements whether they be up or down. This is supported by the January 26, 2009 Levelized Energy Adjustment Clause Order from the PUC which stated:

“Any accepted changes in the calculation of the LEAC factor relative to valuation of GPA's fuel inventory...will only be applicable for the upcoming LEAC period on a one time basis.”

GPA believes this confirms the PUC had the same understanding of the agreement as GPA – that the \$64.46/bbl threshold would be used one time and the basis for the recovery of fuel inventory carrying costs would be reset at the end of the LEAC period (7/31/09). Accordingly, GPA included in its filing for the recovery of approximately \$640,000 for the forecast increase in fuel prices from August 1, 2009 through January 31,

2010. The Georgetown filing has reduced the amount of the recovery by reinstating the \$64.46 threshold.

GPA does not believe the \$64.46 threshold was in mind when the January stipulation was signed and GPA does not believe there is a basis to continue to rely on \$64.46 as an arbitrary threshold over which inventory costs may be recovered and under which they may not.

However, the fact remains that the fuel markets remain highly volatile at this time and there is no clear direction in which the market is moving. Further, GPA has not had an opportunity to discuss these LEAC developments with the CCU. GPA's calculations show that utilization of the July 7 forward curve would reverse the LEAC decrease previously approved by the CCU and would require a small increase in the LEAC rate. GPA is reticent to support such a change without the consent of the CCU, especially at a time when there is so much volatility and uncertainty in the fuel markets. Therefore, GPA believes that of the two factors on the record at this time, the proposed GCG factor represents the best representation of future rates, however, GPA does not agree with the approach utilized to derive the factor. Therefore, GPA wishes to reserve the right to address the situation of the fuel inventory adjustment and petition for a true up of actual inventory carrying cost changes at a later date. GPA believes there is precedent in the setting of LEAC factors for cost recoveries such as this to be spread across more than one LEAC period. GPA wishes to make it clear that the acceptance of the GCG LEAC factor does not in any way represent an agreement with the utilization of \$64.46/bbl as a threshold below which carrying cost adjustments cannot be recovered or paid out. GPA believes the intent of the January 26, 2009 PUC Order was for the fuel inventory carrying cost adjustment to be reset at the end of the LEAC period ending July 31, 2009.

Please don't hesitate to contact me should you have any comments or questions regarding this matter.

Yours truly,



JOAQUIN C. FLORES, P.E.
General Manager

cc: William J. Blair, Esq.
Georgetown Consulting Group
Randall V. Wiegand, GPA CFO
D. Graham Botha, GPA Legal Counsel