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Via Electronic Mail and U.S. Mail

Commissioner Susan Ackerman
Commissioner John Savage
Public Utility Commission of Oregon
550 Capitol St. NE
Salem, Oregon 97301-2551

RE: PacifiCorp Advice No. 11-011

Dear Commissioner Ackerman and Commissioner Savage:

PacifiCorp urges the Commission to allow Advice No. 11-011 to become effective on July 27, 2011. Commission staff recommends the Commission suspend the Advice Filing and initiate an investigation. Alternatively, staff recommends the Commission allow the Advice Filing to become effective subject to an investigation and possible refund. A number of interested parties have commented and recommend the Commission either reject the Advice Filing outright or suspend and investigate. PacifiCorp does not oppose an investigation. PacifiCorp does oppose rejection of the Advice Filing. If the Commission decides to suspend and investigate, PacifiCorp recommends that the Commission advise qualifying facilities (QFs) that some Schedule 37 power purchase agreements (PPAs) entered into during the investigation may ultimately prove to be in violation of PURPA and void *ab initio*.

The Need to Revise Schedule 37

As the Commission is aware, PacifiCorp is required to buy net output from certain QFs at rates published in Schedule 37. The published rates are intended to represent PacifiCorp's full-avoided cost.[1] Under federal law, PacifiCorp cannot be compelled to pay more than its full-avoided cost for QF output.[2] Any QF purchase agreement which has the effect of causing a public utility to pay more than its full-avoided cost is void *ab initio*.[3]

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[1] OPUC Order No. 05-584, 32, 34, 59 (ordering utilities to include a "Fixed Price Method" in QF tariffs that "would remit a total avoided energy cost").

[2] *American Paper Institute, Inc. v. American Electric Power Service Corp.*, 461 US 402, 413 (1983) (PURPA "sets full avoided cost as the maximum rate that the Commission may prescribe"); accord, *Independent Energy Producers Association v. California Public Utilities Commission*, 36 F.3d 848, 850 (9th Cir. 1994); *see also Connecticut Light and Power Company*, 70 FERC ¶ 61,012, 61,029 (1995) (state imposed rates for purchase of QF output which exceed the purchasing utility's avoided cost violate PURPA and FERC regulations).

[3] *Connecticut Light and Power Co.*, 70 FERC ¶ 61,012 at 61,029 ("[I]f parties are required by state law or policy to sign contracts that reflect rates for QF sales at wholesale that are in excess of avoided cost, those contracts will be considered to be void *ab initio.*").

Five QFs currently seek to sell power to PacifiCorp under Schedule 37 (the "Load Pocket QFs").[4] Each of these QFs will deliver power to a location where there is not enough local load to absorb all of the QF output at all times.[5] In each case, PacifiCorp will need to purchase transmission service from the Bonneville Power Administration (or other third party) to move some or all of the QF output to additional PacifiCorp load.[6]

If PacifiCorp is required to purchase net output from the five Load Pocket QFs at Schedule 37 published rates **and** also must pay for third-party transmission to move such output to load, then PacifiCorp will effectively be required to pay more than avoided cost for the output of the five Load Pocket QFs. This is true because Schedule 37 published rates represent PacifiCorp's full-avoided cost and the addition of third-party transmission costs would—as a simple arithmetic truth—raise PacifiCorp's cost above avoided cost.[7] PacifiCorp is concerned that, under these facts, application of existing Schedule 37 to the Load Pocket QFs will lead to PPAs which violate PURPA and are therefore void *ab initio*.

Overview of Changes Proposed

PacifiCorp filed Advice No. 11-011 to address this concern and to clarify that PacifiCorp is not required to pay more than full-avoided cost to purchase QF output under Schedule 37. The Advice Filing proposes targeted changes to Schedule 37. These changes recognize that once a QF and PacifiCorp's merchant function (Merchant) execute a Schedule 37 PPA, Merchant must apply to PacifiCorp's transmission function (Transmission) to designate the QF as a network resource (NR). Under Advice No. 11-011, Transmission is required to determine as part of the NR designation whether the QF's output will cause local generation to exceed local load (an Excess Generation Event) and to determine whether Merchant will need third-party transmission to move such excess generation to load.[8] If Transmission concludes

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[4] *See* Affidavit of Bruce Griswold in Support of Advice No. 11-011 at ¶5.

[5] *Id.*

[6] PacifiCorp would not need to purchase BPA transmission if the Load Pocket QFs would agree to limit their output so as not to exceed local load. However, PacifiCorp has no clear right under PURPA or Schedule 37 to compel such a result.

[7] As discussed in the initial Advice Filing, the delivery of QF excess generation to a load pocket systematically results in an increase in cost because location of a QF in a load pocket does not provide offsetting savings in cost to transmit electric power to load in the load pocket. *See* PacifiCorp's Memorandum in Support of Advice No. 11-011 at 11-12.

[8] After careful consideration, PacifiCorp chose this approach for two reasons. First, this approach allows the determination to be made by Transmission rather than by Merchant. Merchant is responsible for purchasing QF output. Transmission is responsible for providing Network Integrated Transmission Service to Merchant on a non-discriminatory basis. Transmission, as Merchant's native transmission service provider, is the party best situated to determine if third-party transmission will be necessary to move some or all of a QF's output to load. Second, any determination made prior to network resource designation is necessarily provisional because Merchant has no vested right to claim existing capacity on the PacifiCorp transmission system for use to move QF output until those rights have vested with regard to particular QF output at the time the QF is designated as a network resource. PacifiCorp would have preferred a process that definitively identifies whether the *excess generation/third-party transmission problem* exists sooner in the Schedule 37 process, however, because any

Merchant will need third-party transmission, then either: (1) the QF must agree to pay for the required third-party transmission; or (2) the parties (Merchant and the QF) may reach some mutually agreeable alternative solution; or (3) the Schedule 37 PPA will terminate—and the QF may seek a negotiated PPA under PacifiCorp's Oregon Tariff Schedule 38.[9]

The Public Interest is Best Served by Allowing Advice No. 11-011 to Become Effective Subject to Investigation

Commission staff's recommendation to suspend the Advice Filing during an investigation has a certain appeal. It would arguably preserve the *status quo* while the Commission considers whether PacifiCorp has identified a legitimate problem and proposed a legitimate solution. However, suspension of the Advice Filing may actually increase uncertainty for affected QFs. PacifiCorp has asserted that a Schedule 37 PPA violates PURPA and is therefore void *ab initio* if PacifiCorp must both pay full-published avoided cost rates and pay for third-party transmission required to move some or all of the QF's output to load. As a result, there will be uncertainty regarding the legality and enforceability of any Schedule 37 PPA that involves third-party transmission and is executed during the Advice Filing investigation.[10] Given this uncertainty, such a PPA is unlikely to support project financing.

On the other hand, if the Commission allows Advice No. 11-011 to become effective and then initiates an investigation with the possibility of rollback and refund, at least there will be an interim process for identifying which Schedule 37 QFs trigger the *excess generation/third-party transmission* concern. In addition, QFs that are affected will know the cost to proceed if they agree to pay for third-party transmission. Some projects would be economic even with the obligation to pay third-party transmission costs. In such cases, the developer could agree to pay for such transmission (subject to the possibility of retroactive adjustment) and proceed notwithstanding the investigation. If the Commission ultimately rejects PacifiCorp's arguments and requires a rollback of Advice No. 11-011, then the QF would enjoy an improvement in its circumstances. If the Commission ultimately agrees with PacifiCorp and allows Advice No. 11-011 to stand, the developer will have already obtained its long-term PPA consistent with the new requirements. By allowing Advice No. 11-011 to become effective, at least provisionally, the Commission can eliminate the risk of parties entering into contracts that must later be recognized as void.[11]

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such early determination would be necessarily provisional, PacifiCorp has proposed that the determination be made as part of the network resource designation process.

[9] *See* PacifiCorp's Memorandum in Support of Advice No. 11-011 at 7-8.

[10] *See e.g. Southern California Edison Co. v. Public Utilities Com.*, 101 Cal.App.4th 982, 998-999, 125 Cal. Rptr. 2d 211 (2002) ("[I]f the evidence shows that the formula in Decision No. 01-03-067 should have been applied retroactively to arrive at a more accurate SRAC, then it is the Commission's duty to apply it retroactively. The Commission does not have the power to thwart Congressional intent by having a policy inconsistent with that set forth in PURPA.").

[11] PacifiCorp estimates that the cost of third-party transmission required to facilitate output from the Load Pocket QFs is in the neighborhood of $8-9 Million net present value for the 20-year term of the agreements. This effectively becomes the "amount in controversy" with regard to the Load Pocket QFs. This amount represents a roughly seven percent premium above PacifiCorp's full avoided cost.

Because Advice No. 11-011 provides a solution that decreases uncertainty during the investigation period, PacifiCorp urges the Commission to allow the Advice Filing to become effective subject to investigation and possible rollback and refund. However, if the Commission decides to suspend the Advice Filing during an investigation, PacifiCorp recommends the Commission put QF developers on clear notice of the possibility that certain Schedule 37 PPAs enter into during the investigation period may ultimately be determined to be in violation of PURPA and therefore void *ab initio*.

Interested Party Objections to Advice No. 11-011

Interested parties have filed comments opposing the Advice Filing. One gets the impression that commenting parties have thrown out every objection they could dream up—without regard to the underlying problem—in an attempt to make the Advice Filing appear to be absurd, unnecessary, and unworkable. However, PacifiCorp has proposed Advice No. 11-011 in good faith after careful consideration in the face of actual PPA requests which threaten to impose costs on PacifiCorp and its customers in excess of the maximum rate allowed by federal law.

PacifiCorp readily acknowledges that there is more than one way to address the problem. For example, the Commission could simply decide that small QFs which will cause PacifiCorp to need to obtain third-party transmission are no longer eligible for Schedule 37 PPAs and must negotiate a PPA under Schedule 38. This approach would allow the parties to negotiate a rate that is sensitive to the precise cost impact associated with a particular QF's potential for excess generation requiring third-party transmission (or occasional curtailment). However, in proposing Advice No. 11-011, PacifiCorp has attempted, through minimal revisions to Schedule 37, to provide for continued Schedule 37 rights for all small QFs. PacifiCorp is confident that as Commission staff, interested parties, and the Commission investigate the Advice Filing and develop a better understanding of the rational underlying the proposed changes to Schedule 37, they will find that PacifiCorp has made a good faith effort to establish a balanced and workable solution to the problem.

Some commenting parties have objected that the Advice Filing imposes a solution that would require QFs to pay for third-party transmission when easier, more cost effective solutions may exist on a case-by-case basis. PacifiCorp notes that its proposed changes create a backstop solution that insures Schedule 37 PPAs do not violate PURPA. This backstop does not prevent the parties from agreeing to more cost-effective or otherwise desirable solutions nor does it prevent a QF from seeking a PPA under Schedule 38 and negotiating an avoided cost rate that is customized to the realities of its project.

Some commenting parties have urged the Commission to reject Advise No. 11-011 outright. This recommendation appears to be based on the assertion that the issues raised by Advice No. 11-011 were already raised by PacifiCorp and rejected by the Commission in UM 1129. This assertion is inaccurate. During UM 1129, PacifiCorp proposed more flexibility in Schedule 37 pricing. As an argument in favor of greater flexibility, PacifiCorp staff raised by way of example the integration costs that might arise if a 10 MW project is developed in a 5 MW load pocket and PacifiCorp is required to expend funds to move the QF output to load.

Commission staff countered that this hypothetical ignored the fact that a QF located near load might also reduce costs by alleviating the need to import power into a load pocket. The Commission did not purport to decide the merits of the load pocket hypothetical debated by PacifiCorp and Commission staff. Nevertheless, the Commission ultimately decided not to allow for additional flexibility in Schedule 37 pricing. The Commission concluded that if specific issues arise that lead to pricing distortions that should be addressed by adjustments to Schedule 37 rates, the utility should bring such issues to the Commission's attention so they can be examined and bounded. The Commission noted as part of making this decision not to allow for greater flexibility in Schedule 37 pricing, that it was likely to take up the question of integration costs in a later phase of the UM 1129 proceeding.[12] However, the Commission never did so.

Through Advice No. 11-011 PacifiCorp now brings the question of third-party transmission costs to the Commission to be considered, addressed, and bounded. The question is no longer a hypothetical, nor merely an argument advanced by PacifiCorp in support of a request for general flexibility in Schedule 37 pricing; rather it is a specific request for a specific change in the Schedule 37 process intended to address the potential impact of actual pending requests for Schedule 37 PPAs. Without the change proposed by PacifiCorp, those requests threaten to result in Schedule 37 PPAs which violate PURPA and are therefore void *ab initio*. In sum, the question raised in Advice No. 11-011 should not be summarily dismissed because it has not been previously asked and answered in UM 1129 or in any other context. There is no credible theory of *res judicata* or other principle of finality that would bar PacifiCorp or the Commission from considering this important issue at this time.

Conclusion

PacifiCorp appreciates the opportunity to present its views to the Commission and looks forward to working with the Commission, its staff, and all interested parties to implement revisions to Schedule 37 and to continue to improve its QF program.

Sincerely,

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[12] The Commission noted, in Order No. 05-584 that "certain issues, such as integration costs, will likely be taken up during the second phase of this investigation when interconnection procedures and agreements will be addressed."