Q. PLEASE STATE YOUR NAME AND POSITION.

A. My name is Maury Galbraith. The Public Utility Commission of Oregon ("OPUC") employs me as a Senior Economist. My qualifications are shown on Exhibit Staff/101, Galbraith/1.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. The purpose of my testimony is to present Staff's adjustments to Portland General Electric's (PGE's) forecast of net variable power costs (NVPC) for 2005. In PGE's 2005 Resource Valuation Mechanism filing (Docket UE 161), the company forecast NVPC at $492 million.

Q. WHAT ARE STAFF'S ADJUSTMENTS?

A. Staff proposes a disallowance of the above-market costs associated with four purchase contracts signed by PGE between 28 and 35 months prior to the start of delivery.

Q. WHAT IS THE DOLLAR IMPACT OF THIS DISALLOWANCE ON PGE'S FORECAST OF NVPC FOR 2005?

The impact is a $7.172 million decrease to the forecasted NVPC included in the company's filed case.

Q. PLEASE IDENTIFY THE FOUR DISPUTED CONTRACTS.

A. The four disputed contracts are identified in Table 1.

Table 1. Disputed Contracts.

Counter Party	Deal #	Transaction Date
Mirant Americas Energy Marketing, L.P.	1270	01/29/2001
Morgan Stanley Capital Group, Inc.	2765	06/12/2001
Morgan Stanley Capital Group, Inc.	3497	08/09/2001
El Paso Merchant Energy, L.P.	3593	08/16/2001

The four contracts provide a total of 100 megawatts of flat delivery for calendar years 2004-2006 and were signed by PGE between 28 and 35 months prior to their January 1, 2004 start dates.

Q. ARE THESE THE SAME FOUR CONTRACTS THAT RECEIVED A PRUDENCE DISALLOWANCE IN ORDER 02-772?

A. No. However, the facts in this case closely resemble those debated in docket UE 139.

Q. PLEASE DISCUSS THE FACTUAL SIMILARITIES BETWEEN THE TWO CASES.

A. First, in UE 139 it was clear that PGE had acted outside its routine practice. Since the mid-1990's the company's general practice had been to begin filling its net open position 12 to 18 months prior to delivery. PGE based this practice on the period over which markets were expected to be liquid. The contracts for which the Commission made a prudence disallowance in Order 02-772 were signed between 19 and 23 months prior to delivery. The contracts being contested in this current docket UE 161 were signed 28 to 35 months prior to delivery. Second, the UE 139 contracts were signed prior to the market achieving liquidity. The UE 161 contracts were also signed without market liquidity or reference to "like transactions". Third, in UE 139 PGE failed to provide information and analysis that could have established the reasonableness of its actions. The evidence PGE provided did not allow the Commission to reach the conclusion that PGE's actions were prudent. In UE 161, PGE has again failed to provide evidence to justify its purchases.

Q. DOES PGE ARGUE THAT IT ACTED INSIDE ITS ROUTINE PRACTICE WHEN IT SIGNED THE DISPUTED CONTRACTS MORE THAN TWO YEARS PRIOR TO DELIVERY?

A. Yes. In direct testimony, Mr. Lobdell explains that PGE's routine practice is to buy small increments of power over long periods of time. Mr. Lobdell states:

> "Pending the acquisition of long-term resources, we have determined that the most reasonable way to purchase this required power is to buy small increments over a long period of time, subject to market constraints such as liquidity. This process is similar to "dollar cost averaging" that financial advisors recommend for small investors. We are not able to time the power markets any more than small investors can time the stock or bond markets." UE 161/PGE 200/Lobdell/9.

In addition, Mr. Lobdell explains that PGE cannot and should not always wait for market liquidity when building its power portfolio. Mr. Lobdell states:

> "Making purchases only when the market is clearly liquid would result in PGE making large block purchases close in time to the date of delivery, thereby jeopardizing reliability and significantly increasing the volatility of our costs." UE 161/PGE 200/Lobdell/9.

Q. DO THE DISPUTED CONTRACTS REFLECT THE CONSISTENT APPLICATION OF PGE'S STRATEGY TO BUILD ITS PURCHASED POWER PORTFOLIO IN SMALL INCREMENTS OVER A LONG PERIOD OF TIME?

A. No. Exhibit Staff/102, Galbraith/1 shows PGE's power purchases with 2005 delivery in megawatt hours by transaction date. Exhibit Staff/102, Galbraith/2 shows the extended cost of these purchases by transaction date. These exhibits demonstrate two facts. First, there is a lack of regularity to PGE's power purchasing for 2005. PGE purchased power for 2005 on 5 days in 2001. The last purchase in 2001 was on September 27th. PGE did not enter into another transaction for 2005 power until February 17, 2004. PGE then purchased power for 2005 on 30 days between February 17, 2004 and June 3, 2004. Second, the disputed contracts are clear outliers. These contracts not only stand out due to their transaction dates, but also standout in terms of amount of power purchased and cost.

Q. SHOULD THE COMMISSION BE CONCERNED BY THE LACK OF REGULARITY IN PGE'S POWER PURCHASING FOR 2005?

A. Yes. Although Staff did not expect to find that PGE had purchased the same fixed amount of power every month or quarter, or that PGE had extended the same dollar amount of power every month or quarter, we did expect to see periodic purchasing. Financial advisors that recommend "dollar cost averaging" stress the critical importance of sticking with the plan no matter how good or bad the current financial news. Without periodic purchasing, PGE's strategy for filling its net open position loses much of its risk reduction benefit.

Q. HOW DOES PGE EXPLAIN THE LACK OF PURCHASES IN EITHER 2002 OR 2003?

A. PGE claims that there were limited opportunities to buy power for 2005 that far in advance of delivery. UE 161/PGE 200/Lobdell/9.

Q. DOES STAFF BELIEVE PGE ACTED OUTSIDE ITS ROUTINE PRACTICE WHEN IT SIGNED THE DISPUTED CONTRACTS?

A. Yes. First, the disputed contracts were signed 28 to 35 months prior to delivery. PGE’s routine practice was to begin filling its net open position 12 to 18 months prior to delivery. I discussed PGE's advance purchasing rule-of-thumb in direct testimony in docket UE 139. UE 139/Staff 100/Galbraith/1-5. Second, the UE 161 contracts do not appear to be part of a disciplined strategy to make periodic power purchases. The UE 161 contracts are outliers on both counts.

Q. DOES PGE ARGUE THAT THE MARKET FOR 2004-2006 POWER PRODUCTS WAS LIQUID AT THE TIME IT SIGNED THE DISPUTED CONTRACTS?

A. No. In direct testimony in Docket UE 149, the company suggested that these contracts are structured products not standard term purchases. According to PGE, structured products are to be compared to alternative products and services, whereas standard term purchases are to be compared to 'like transactions'. UE 149/PGE 200/Lobdell/21-22.

Q. DOES STAFF AGREE WITH PGE THAT THE DISPUTED CONTRACTS ARE STRUCTURED PRODUCTS?

A. Not completely. Staff addressed this issue in direct testimony in Docket UE 149. UE 149/Staff 100/Galbraith/19-24. On perhaps the most important criterion, shaping and unique characteristics, the disputed contracts look more like standard term purchases than structured products. All four of the transactions are 25 MW block products with flat delivery (i.e., no shaping).

Q. DID PGE'S STRUCTURING GROUP ANALYZE AND EXECUTE THE DISPUTED TRANSACTIONS?

A. No. In PGE Response to OPUC Data Request No. 49 in Docket UE 149, the company explained that the Structuring Group was formalized in March of 2001. The first disputed contract (Deal No. 1270) was done before this group was created. The Structuring Group was not involved in analyzing the other disputed contracts (Deal Nos. 2765, 3497, and 3593) because the group was initially tasked with developing modeling tools for evaluating non-standard products.

Q. DOES STAFF AGREE WITH PGE THAT STRUCTURED PRODUCTS AND STANDARD TERM PURCHASES SHOULD BE EVALUATED IN DIFFERENT WAYS?

A. No. All purchases, both standard term purchases and structured products, should be compared to the available alternatives. A liquid market with many 'like transactions' simply represents a readily available alternative. For block products with little or no shaping a comparison with the market alternative is straightforward. The difficultly with structured products is that their unique characteristics often make a comparison with the market alternative difficult. In either case, the proper method of evaluation is to compare the product under consideration to the available alternatives.

Q. HAS PGE PROVIDED ANY STUDIES OR ANALYSES DONE AT THE TIME THE DISPUTED CONTRACTS WERE SIGNED THAT COMPARED THE TRANSACTIONS TO OTHER ALTERNATIVES?

A. No.

Q. HAS PGE PROVIDED ANY STUDIES OR ANALYSES DONE AT THE TIME THE DISPUTED CONTRACTS WERE SIGNED THAT INDICATE SUPPLY WOULD BE TIGHT IN 2004-2006?

A. No.

Q. HAS PGE PROVIDED INFORMATION OR ANALYSIS FROM THE TIME IT SIGNED THE DISPUTED CONTRACTS THAT CAN ESTABLISH THE REASONABLENESS OF THE COMPANY'S ACTIONS?

A. No.

Q. SHOULD THE COMMISSION DISALLOW THE ABOVE-MARKET COST OF THE FOUR DISPUTED CONTRACTS?

A. Yes. The contracts being contested in docket UE 161 were signed 28 to 35 months prior to delivery. It is clear that PGE acted outside its routine practice. PGE has failed to provide any information or analysis that justifies its deviation from routine practice or that establishes the reasonableness of its actions. Staff's view of these contracts remains unchanged from last year's RVM proceeding.

Q. WHAT PROXY PRICE METHODOLOGY DOES STAFF RECOMMEND THE COMMISSION USE TO CALCULATE A DISALLOWANCE?

A. Staff recommends the same proxy price methodology that it proposed in last year's RVM. UE 149/Staff 100/Galbraith/23-24. Staff recommends that the Commission use the price of Deal No. 3497 as the proxy price. The Deal No. 3497 price is the lowest price of the disputed transactions. This represents a reasonable proxy price and a conservative methodology.

Q. WHY DOES THIS REPRESENT A CONSERVATIVE APPROACH?

A. It is a conservative approach because it does not include a disallowance for Deal No. 3497.

Q. DID STAFF CONSIDER ALTERNATIVE PROXY PRICES?

A. Yes. Staff considered using PGE's forward price curve from July 1, 2003 (i.e., eighteen months prior to the start of delivery) as a proxy price. We did not recommend the use of this methodology in last year's RVM. UE 149/Staff 100/Galbraith/23. For the same reasons, Staff continues to oppose this methodology. Staff considered using the price from PGE's earliest transaction with flat delivery during 2005 signed within the eighteen-month timeframe as a proxy price. We also considered using a comparable flat product average price based on PGE's undisputed power purchases with 2005 delivery as a proxy price. These last two methodologies rely on information determined after the fact to set the proxy price. Commission prudence reviews are based on what was reasonable and known at the time of the disputed action. For this reason, Staff opposes the use of these proxy prices.

Q. WHAT IS THE OVERALL IMPACT ON PGE'S FORECAST OF 2005 NVPC OF RE-PRICING THE DISPUTED CONTRACTS USING THE DEAL NO. 3497 PRICE?

A. Staff's recommended approach results in a disallowance of $7.172 million. Exhibit Staff/103, Galbraith/1 shows the details of the calculation.

Q. DOES STAFF RECOMMEND THAT THE COMMISSION USE THE SAME METHODOLOGY TO RE-PRICE THESE TRANSACTIONS IN THE 2006 RVM PROCEEDING?

A. Yes.

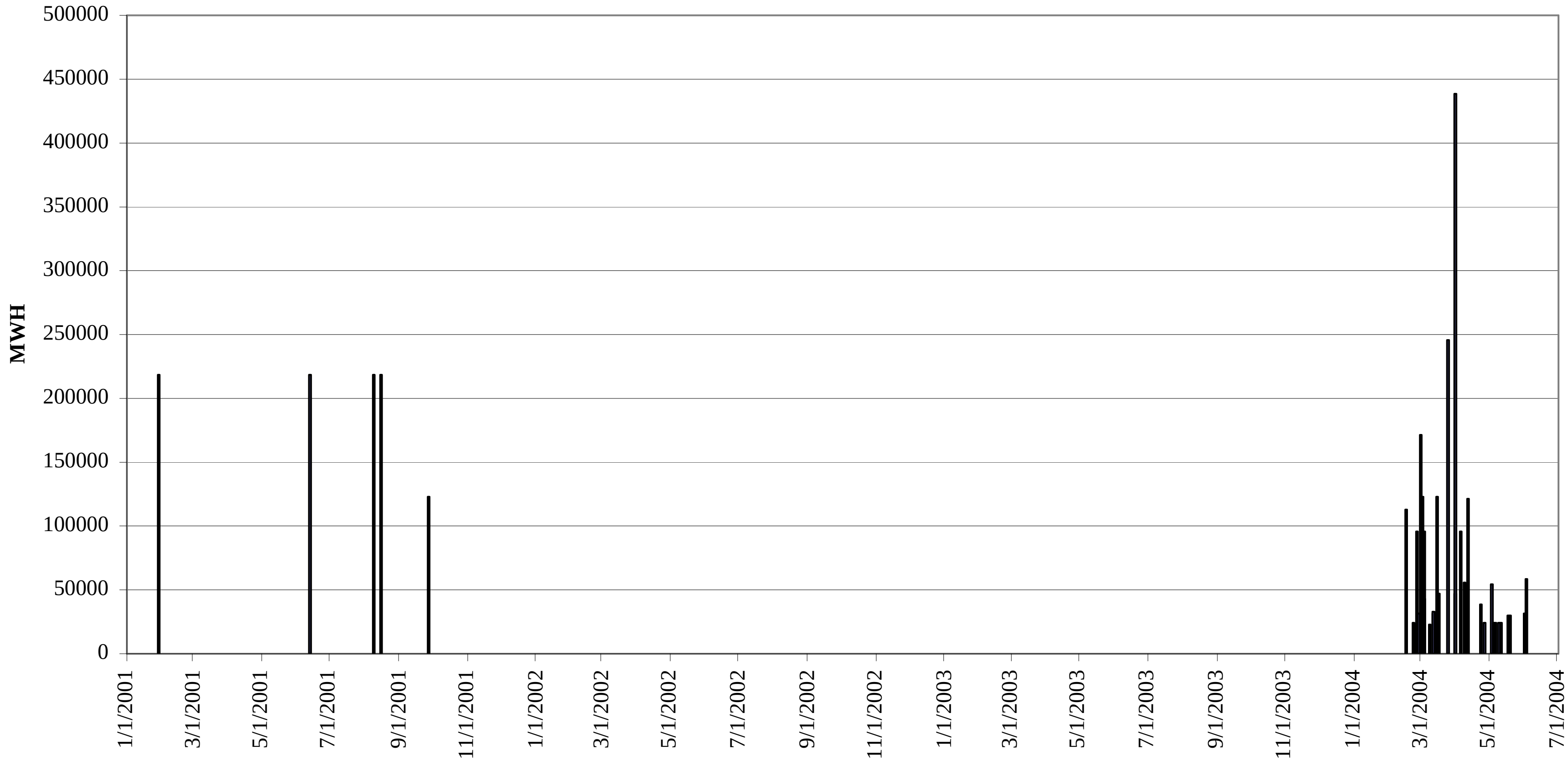
Q. DOES STAFF HAVE ANY OTHER ADJUSTMENTS TO PROPOSE IN UE 161?

A. No.

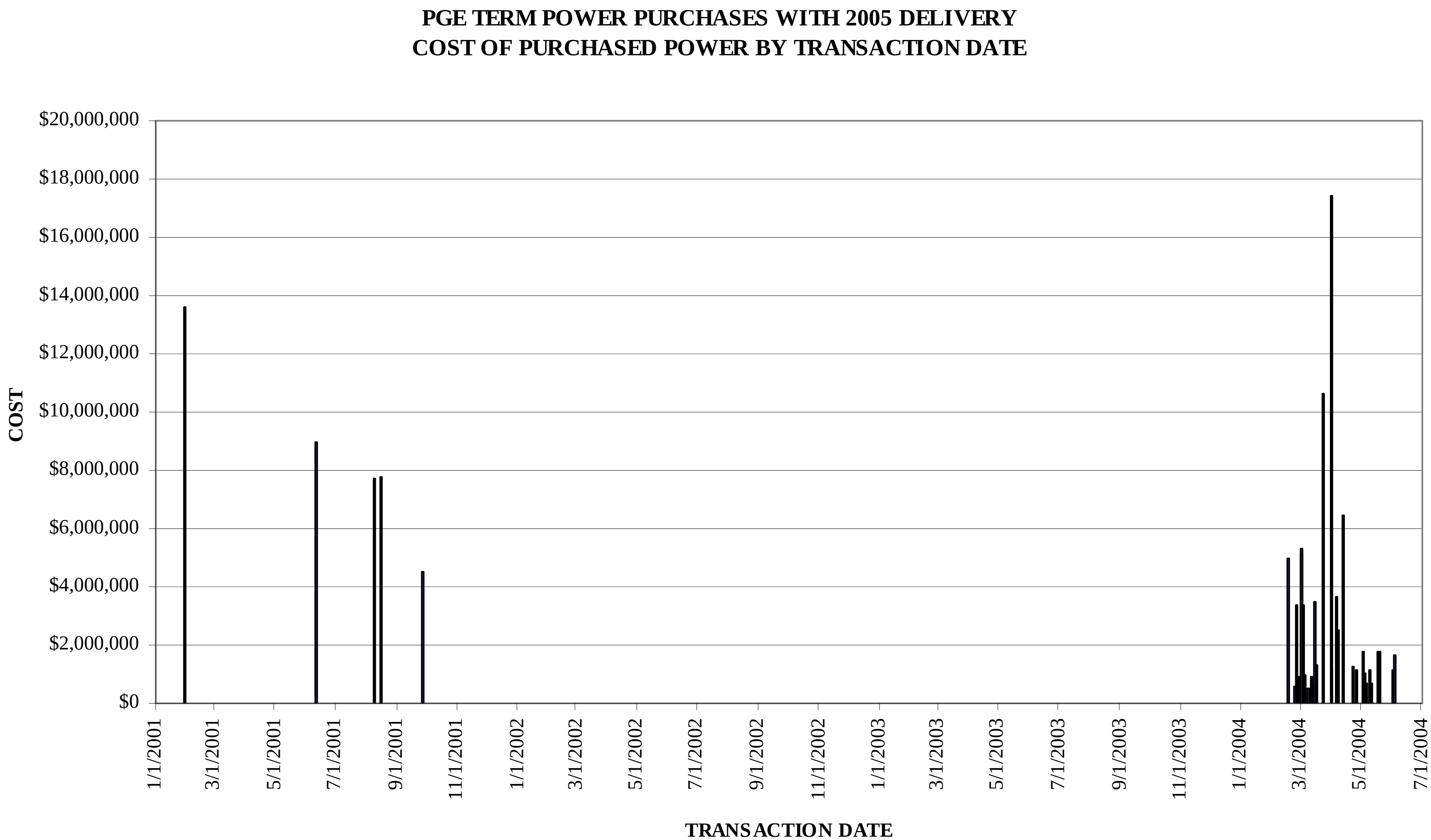
Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

PGE TERM POWER PURCHASES WITH 2005 DELIVERY
MWH PURCHASED BY TRANSACTION DATE



Note: Excludes BPA Wind Purchase on 4/22/2001 and SB 1149 Index Purchases on 4/28/04 and 5/20/2004.
Data Source: UE 161 PGE Response to OPUC Data Request 13.



Note: Excludes BPA Wind Purchase on 4/22/2001 and SB 1149 Index Purchases on 4/28/04 and 5/20/2004.
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