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Oregon Public Utility Commission
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Re: Docket No. UM 1182

Enclosed for filing is one copy of PacifiCorp's Reply Comments in this matter. A hard copy was served on all parties of record as indicated on the attached certificate of service.

Very truly yours,

Katherine A. McDowell

KAM:jlf
Enclosure
cc: Service List

BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON

UM 1182

In the Matter of an Investigation Regarding Competitive Bidding	**PACIFICORP'S REPLY COMMENTS**

PacifiCorp hereby respectfully submits its reply comments. Responses specific to the opening comments of the Oregon Public Utility Commission (the "Commission") Staff ("Staff") are in Section I and responses specific to the opening comments of other parties to this docket are in Section II.

I. RESPONSE TO STAFF'S COMMENTS

A. Guideline 2: RFP Requirement

In its Opening Comments at 3, Staff explains that it arrived at its greater than 5-year and greater than 50-MW Major Resource definition by reviewing the energy risk management policies of Oregon's investor-owned electric utilities. According to Staff, this review showed that transactions with delivery terms greater than 48 months generally require prior approval by senior management. *Id.* It follows, Staff reasoned, that duration must therefore define a "significant energy resource". *Id.* Staff has since explained to PacifiCorp (in an October 14, 2005 telephone conversation) that Staff is currently evaluating whether to increase the quantities trigger to 100 MW in its Reply Comments. PacifiCorp notes that other parties' comments, including the joint opening comments of the Citizens' Utility Board, Renewable Northwest Project and Northwest Energy Coalition ("Joint Opening Comments") and the opening comments of Portland General Electric, also suggest changing Staff's major resource definition to increase the size to 100 MW. PacifiCorp agrees.

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As explained in more detail in PacifiCorp's Opening Comments at 3-4, a low threshold, such as 5 years and 50 MW, will likely result in higher costs and risk for ratepayers, because such a low threshold establishes a bias towards short-term power purchase agreements ("PPAs") and potentially no development of new assets, and will impair PacifiCorp's ability to actively hedge its position in the liquid forward markets. Moreover, because PacifiCorp operates a 9,000 MW system, a 50 MW resource does not represent a significant resource. Therefore, PacifiCorp urges the Commission to increase the major resource size definition from 50 MW to 100 MW.

In addition, as already set out in its opening comments, PacifiCorp urges the Commission to define the duration portion of the definition as 10 years, rather than Staff's proposed 5 years. PacifiCorp understands Staff's difficulties in deciding how best to define a significant resource, and appreciates Staff's willingness to reconsider the quantities requirement. However, PacifiCorp believes that Staff's underlying reasoning with respect to the proposed 5-year duration is incorrect because Commission-established RFP parameters should not be tied to corporate risk management policies that are subject to change. Corporate risk management policies are internal operational documents that change from time to time depending on factors not necessarily tied to whether or not a transaction involves a significant energy resource. Such factors influencing risk polices may include a utility's risk tolerance which will vary through time as internal and external conditions such as market conditions, capital and cash allocation and counter-party credit requirements vary. These factors do not necessarily depend on the resource being acquired but can vary depending on the individual utility, the type of counter-party (legal structure) and the structure and nature of the specific transactions.

Rather than looking to utility specific documents that can vary over time, PacifiCorp recommends that the Commission look to the IRP because the IRP identifies, in a public setting, significant resources as part of its planning process. Moreover, the Commission and

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other parties have consistently taken the position that the IRP and any resulting RFP process should be better aligned. If the Commission were to approve Staff's 5 year trigger for the RFP, the Commission would create exactly the opposite result, *i.e.* inconsistencies and disconnect, because PacifiCorp's IRP uses a 20-year planning horizon with an Action Plan for the next 10 years.

PacifiCorp's IRP specifically targets long-term supply side resource additions (10 years or more) to meet future needs. It follows that RFPs issued for long-term resources should focus on time horizons that are consistent with those studied in the IRP. The horizons for long-term IRP proxy (significant) resources studied in the IRP are not 5 years as evidenced by Appendix C (Table C.27) to PacifiCorp's most recently filed IRP. In fact, the supply side resource alternative with the shortest design life is 10 years (in the case of customer owned standby generation); most are supply side alternatives of 20 years or more. To the extent that the resource is not identified as a significant resource in the IRP, and as part of the development of an Action Plan, then the utility would consider the length or deficit on the system to be a balancing activity that should not be constrained by a formal and lengthy process intended to address long-term resource additions. The market for significant resources (long-term resources) clearly desires a reasonably transparent process to understand what the utility will use as its benchmark. Indeed, this is a key theme expressed by parties to this docket and PacifiCorp agrees.

Consequently, PacifiCorp proposes that resource and planning horizons should define what constitutes a significant resource in an RFP just like it does in an IRP. PacifiCorp encourages the Commission to align the IRP and the RFP by looking at a term consistent with the long-term planning horizon studied in the IRP.

Moreover, such an approach is consistent with the liquid forward markets available to utilities. (*See* PacifiCorp Opening Comments at 3-4.) These market opportunities do not fit well with lengthy competitive bidding processes and therefore, if a 5-year RFP trigger is mandated, may result in these opportunities being lost to utilities. If these opportunities are lost, then the price risk associated with balancing PacifiCorp's system will increase. As a result, the risk that the cost to ratepayers would be higher would increase as well. No party to this docket has expressed a desire to have an ineffective procurement process for long-term resources. PacifiCorp encourages transparency and will define a benchmark as a means to ensure competitive behavior in the market.

Staff's proposal may also create a bias against resource alternatives based on new assets, either build or purchase agreements from new assets. Bidders have indicated in the past that new asset backed resources are difficult to finance unless some portion of the output is committed for the long term. Entities who are willing to construct new assets indicate a desire for purchase agreements from those facilities with terms greater than 10 years. Consequently, Staff's position would lead to a bias towards PPAs and limit the RFP process and its participation to either power marketers with no assets or wholesale qualified entities with existing assets. Ultimately, this may lead to an increase in costs to utilities and its ratepayers, by artificially restricting the market alternatives because it sets up a scenario where power purchase and new asset build, cannot compete against one another. Therefore, the Commission should establish a process that allows PacifiCorp, and consequently ratepayers, to fully benefit from market opportunities and a level playing field between PPA and asset-backed resources.

B. Guideline 3: Exceptions to the RFP Requirement

It is PacifiCorp's understanding (based on its conversation with Mr. Galbraith) that Staff's RFP exceptions contemplate a process whereby a utility seeking to pursue a resource in the case of an emergency or market opportunity (not involving a self-build or owned option) completes the transaction without prior Commission approval, and that the prudence of such a transaction will be evaluated in the next rate case. A waiver, on the other hand, would only be used when a utility wishes to proceed without an RFP due to requirements or

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circumstances specific to the resource (for example, a joint project with other utilities to build a plant that uses coal as fuel). PacifiCorp understands that Staff is considering removing the "self-build resources" carve-out in the exception guideline; if that is the case, PacifiCorp has no objection to this Guideline.

Alternatively, a waiver process (without any exceptions for major resources), with an opportunity for expedited process where necessary, may also be a reasonable compromise of the parties' positions in this proceeding. PacifiCorp does, however, strongly object to the prohibition on using the exception process for self-build resources for the reasons stated in its opening comments.

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C. Guidelines 8(a) and 12: Utility Benchmark

In its Opening Comments at 5, Staff states that "Staff recommends that selection of an initial short-list of bids be based on price and non-price factors," and that "[t]he non-price score [should] be based on the resource characteristics identified in the utility's IRP Action Plan (e.g., resource duration, dispatch flexibility, portfolio diversity, etc.) and conformance to the standard form contracts attached to the RFP." This language applies to the utility's benchmark via Guideline 12. While Staff does not appear to view the utility benchmark as a bid, Staff apparently does believe that the utility benchmark should be evaluated consistent with bidders using price and non-price factors.

As a general matter, PacifiCorp agrees that any benchmark option is not the same as a bid. That fact should reasonably lead to the conclusion that a utility benchmark option should not be treated the same as a bid. The purpose of the benchmark option is to offer a hedge against the market to protect the utility, and consequently ratepayers. Absent new information being available since the IRP is published, the proxy resource in the IRP will typically be used to identify the benchmark option and resource characteristics identified in the utility's IRP Action Plan[1]. The benchmark, by definition, always gets a full score on non-price factors (not price factors) because it is consistent with the minimum requirements identified in the RFP. Such minimum requirements typical relate directly back to the proxy resource identified in the IRP. For that reason, PacifiCorp questions the value of evaluating a benchmark on non-price factors.

If, however, parties intend to expand the scope of the non-price criteria beyond those criteria previously included in recent RFPs to include factors such as construction cost overrun risk, PacifiCorp must oppose any such proposal. (*See, e.g.*, Northwest Independent Power Producers Coalition ("NIPPC") Opening Comments, Attachment A, Guideline 5(f)).

The benchmark option is a cost-based alternative provided by the utility for the protection of ratepayers and pursuant to the then-current regulatory compact. Under the current regulatory scheme, such options may be evaluated at cost.[2] Under that scenario, PacifiCorp is permitted to earn no more than its authorized rate of return set in comparison to comparable utilities. Likewise, while ratepayers may pay additional costs for the project (if deemed prudent), they will also get the benefit if the utility achieves any cost savings, which savings are generally, not shared with the utility in PPAs. These rules establish a very different economic paradigm than exists for bidders who may offer to take certain types of

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[1] PacifiCorp notes that Staff's example resource characteristics identified in the Action Plan include "resource duration." For all of the reasons previously discussed in PacifiCorp's filings in this docket and in UM 1056, PacifiCorp strongly opposes a requirement to model resource duration in the IRP as impractical and unworkable in advance of knowing what the market will offer. Without repeating all of those comments here, PacifiCorp wishes to direct the Commission to those comments for PacifiCorp's opinion on the issue.

[2] In Order 05-133 in Docket UM 1066, the Commission directed the parties to focus on cost, not market, in proceeding through the investigation under UM 1056. The Commission also held that until the resolution of UM 1066, utilities must file a request for a waiver of the administrative rule when the utility wishes to include a new resource in its revenue requirement at cost, not market. While the order did not explicitly direct parties in UM 1182 to focus on cost, not market, until there is further direction in UM 1066, the cost/market issue is also implicated in this proceeding as it is unclear how the market rule will operate and how, if it all, it would change the return on equity issue discussed above. Accordingly, PacifiCorp's comments are directed at the cost issue.

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risks and therefore, also expect to get much larger returns. If the Commission were to establish a scenario where the benchmark option were to be treated and evaluated like a "bid" (*e.g.*, where cost over or under runs and other similar non-price variables were considered in the first round evaluation), it would create a mismatch between the purpose of the benchmark option, the regulatory paradigm governing that option and the risk profile of the utility in comparison to bidders. Until the regulatory paradigm permits the utility to submit a "bid" on truly the same basis as other bidders, and thus recover greater than its allowed return on equity and/or operational income that exceeds its cost, the utility's cost-based alternative should not be treated the same as a "bid" in the evaluation of such non-price factors.

D. Guideline 8(b): Individual v. Portfolio Analysis

Staff recommends in its Opening Comments at 6 that "selection of the final short-list of bids be based on total system portfolio analysis using the utility's production cost and risk models to identify the best combination of resource additions." It is not entirely clear what type of analysis Staff is proposing in this language. If Staff is proposing that the utility conduct production cost modeling using the same assumptions from its most recent IRP in the selection of the final short-list, PacifiCorp agrees with the proposed language and indeed, in PacifiCorp's Draft 2009 RFP (Docket UM 1208), the Company has included a proposal to conduct this type of analysis.

PacifiCorp does not agree that it is appropriate, however, to redo the analysis of those assumptions in the RFP process. The time for the analysis and public input is in the long-standing and well-defined IRP process which takes place every two years with an update filing provided annually. Further, PacifiCorp does not understand the benefit of duplicating that analysis in two places, which may serve to increase costs to ratepayers or delay the process, with the ultimate result of the process not being successful. For example, some bidders are unwilling to leave bids open for a long period of time without building in a market movement premium or will likely refuse to enter into contracts if the market moves

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against them. As Staff has itself acknowledged, rerunning the IRP modeling, by reconstructing the portfolios, is an exercise in judgment that balances costs and risk—which takes time. The extended evaluation time could result in the utility losing best-price bids, as well as extending the RFP process to unmanageable lengths of time. Instead, the RFP process must tie to the IRP, and it does under the Company's proposal; however, the RFP process should also be a flexible and nimble process that is not overly cumbersome and costly, or does not create barriers to entry by the market.

Finally, if it is Staff's position that a portfolio analysis must include analysis of uneconomic bids, PacifiCorp opposes that proposal for the reasons stated in its Opening Comments. Put simply, the Company will seek to acquire the resources identified in the Action Plan, including those identified as providing value to the portfolio in terms of adding diverse resource options, such as the renewable target. It may do so in the context of single-source RFPs. It would not be appropriate however to require the utility to conduct all-source RFPs for the sole purpose of "adding" otherwise uneconomic bids together with economic bids to achieve the diversity target. Moreover, even if the resources together may be economic, such an approach creates significant practical hurdles in addition to potential prudence challenges in trying to negotiate with two (or more) bidders at the same time in order to achieve the portfolio outcome. If the economic bidder drops out of the process for whatever reason, PacifiCorp would be left with only the uneconomic bid. PacifiCorp believes that the regulatory process in this and its other states will not permit the Company to acquire uneconomic resources without creating serious prudence challenges. Finally, such a proposal might serve as an impediment to the market by not providing a clear signal of what it takes to win the RFP. As recent Federal Energy Regulatory Commission proceedings have made clear, ambiguity in RFPs can serve to chill participation.

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II. COMMENT IN RESPONSE TO OTHER PARTIES' COMMENTS

A. NIPPC Guideline 5: "Benchmark Option"[3]

NIPPC has proposed that the IE "will score all bids separately" from the utility. In contrast, Staff's guideline covering this topic (Guideline 13(b)(ii)) states that the IE will validate the Benchmark Score and "may validate, sample, or independently score all bids, at the discretion of the IE and the Commission." Staff's approach is a more reasonable approach in the RFP context. The IE, at the Commission's direction, should score as many bids as the IE believes are necessary for the IE to be able to reach a professional judgment that the process was fair and the result was reasonable. Based on actual experience, where bidders submit more than one bid changing only a few criteria, it may be possible that the IE, exercising its professional judgment will determine that it is not necessary to score a similar bid because the IE can tell that the bid is not as economic as the other options from that bidder. While PacifiCorp would not object to an IE scoring all bids if that IE believed such a step was necessary, PacifiCorp does not believe the requirement that the IE must score all bids is reasonable or necessary and can only serve to increase the cost to bidders and ratepayers for IE services.

B. Guideline 6: Utility Ownership Options

Both the opening comments of the NIPPC and the Joint Opening Comments propose that Oregon's competitive bidding guidelines should explicitly state that bidders may submit a bid to construct at the utility's site. (*See* Joint Opening Comments Attachment at 2; NIPPC Opening Comments at 12.) PacifiCorp opposes the imposition of such a requirement in all RFPs.

As an initial matter, it is important to point out that it is PacifiCorp's intent to offer its site to bidders when it has a site that is already partially developed and paid for by ratepayers,

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[3] NIPPC's Attachment A uses a different numbering scheme that does not correlate to Staff's Proposed Guidelines.

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and when the bidder is bidding to a specific bid specification which can be adequately outlined in the RFP. To the extent that the utility will own and operate the asset that is the result of an engineering, procurement and construction ("EPC") bid or a build-own-transfer ("BOT") bid, it must be consistent with the specifications of the reference plant in the RFP. It may be appropriate under those circumstances, as suggested by NIPPC, to permit EPC bids or BOT bids. For example, such options are available under RFP 2009 as drafted. However, it simply is not reasonable or prudent to force a utility to own and/or operate any asset that a bidder may choose to offer. This is not in the best interest of customers or the utility and creates risk increasing and overly proscriptive and inappropriate requirement to include in the guidelines.

First, if such a requirement is considered it should be limited to the type of risk the utility should be willing to take at the particular site. EPC and BOT bids provide different risk profiles for the utility, and ultimately, ratepayers. In both cases the utility will be required to own and operate the facility however, the development risks associated with each of them are different. Under an EPC bid, the bidder takes the construction risk, but typically leaves the development risk with the utility. Under a BOT bid, the developer typically takes both the development and construction risk. It is possible that PacifiCorp's analysis may show that it is not a good option for ratepayers to be required to take the development risk at a certain site depending on the site-specific characteristics. There are many variables that must be taken into account when considering if bidders should be allowed to bid the utility's site. Key amongst these are site-specific risks (such as development) and resource-specific operational or infrastructure criteria. A requirement that the utility always permit EPC bids on its site could easily result in ratepayers being inappropriately exposed to risks that cannot effectively be managed or hedged (risks including but not limited to environmental, water availability, permitting and wetland issues).

Moreover, a utility-developed site may provide best value to ratepayers if it is utilized to its fullest potential (then or in the future). A utility develops its sites with a certain size of resource in mind taking into account water availability, air permit restrictions, fuel, and other critical development issues such as potential future use. If a site could be developed to accommodate a large project (*e.g.* 500 MWs or more), the value of the site will be diluted for ratepayers if there are no restrictions on the size of the project a bidder can offer to build on the site. Also, if the resources at the utilities sites are each different then, integration, operation, maintenance and interconnection may become a problem.

Similarly, if the utility is accepting BOT and EPC options at the utility site (as well as PPA options), it is important that the bidders build to the engineering specifications provided by the utility. If not, the utility cannot reasonably expect to acquire a plant at the end of the process that can operate in a manner that is best integrated with the utility's system. For example, PacifiCorp may specify in engineering specifications that certain types and standards of equipment be used in the construction process. Such a requirement offers value to ratepayers because the utility may have the same type of equipment at other sites which it can physically utilize in emergencies or its crews may be better trained to maintain and/or repair. Also, in these situations, it is the utility and ratepayers, not the EPC or BOT bidder, who has the long-term commitment to the plant and therefore, specifications and quality, are critically important. Such a requirement also provides benefits to bidders as it provides a high degree of transparency, allows bidders to be compared on the merits of their competitiveness (rather than potentially undesirable design alternatives), and provides customers with the further benefit of having such bids compared from a common set of specifications.

The magnitude of these issues and costs are greatly increased when fuel-type is taken into consideration. For example, for a coal plant benchmark option, the timeline is longer

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and the cost and complexity is greater for permitting and specifications related to the utility site.

Finally, PacifiCorp may not have a site to include, for example in the most recent renewable resource RFP. Therefore, if this were to be made a requirement, it should be limited to situations where a site is available for use.

The proposed guideline fails to take any of these variables into account requiring instead just a blank offering of the utility site without any cautionary restrictions. It would provide more value to ratepayers to consider these options on an RFP by RFP basis. Therefore, PacifiCorp believes that a far better approach to this proposed issue is to leave the consideration of whether to permit bidding on the utility site to the review of the draft RFP. The utility could include an explanation with its filing explaining why it chose to include or not include such an option. To the extent a potential bidder has a strong value proposition for customers, the potential bidder is afforded the opportunity to comment during the public comment period.

C. Guideline 8(c): Debt Imputation

Some parties have taken issue with the way in which Staff proposes to use imputed debt as an evaluation criterion. (*See* NIPPC Opening Comments at 10-12; Industrial Customers of Northwest Utilities ("ICNU") Opening Comments at 9-10; Joint Opening Comments at 4-5.) PacifiCorp assumes that there is no dispute regarding direct debt (*e.g.*, debt directly applied on PacifiCorp's financial books as a result of accounting standards), because all parties who commented on the issue are focused only on imputed debt. This lack of comment on direct debt is unremarkable given that the thrust of the parties' comments is a question of subjectivity with respect to imputed debt that cannot reasonably be argued to even exist with respect to direct debt. Accordingly, PacifiCorp requests that the Commission recognize the consideration of direct debt on any bid that results in such an accounting designation.

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With respect to imputed debt, as already explained in PacifiCorp's Opening Comments at 9-10, imputed debt can impose a very real cost on ratepayers that should be factored, consistent with the application of the cost of direct debt, as part of the first round of the resource evaluation process. Imputed (also referred to as "inferred") debt results when credit rating agencies infer an amount of debt associated with a power supply contract (inclusive of PPAs) and take the added debt into account when reviewing the utility's credit standing. This is due to the fact that the fixed charges associated with power supply contracts increase the utility's financial risk in the same way that long-term debt and other financial obligations increase financial risk. Consequently, investors, as well as regulators and the accounting profession, regard the fixed obligations associated with such contracts as being equivalent to debt.

There are readily identifiable and verifiable methods of calculating the imputed debt associated with PPAs and other contracts. Standard & Poor's Corporation ("S&P"), for instance, has determined specifically for PacifiCorp that a 50 percent risk factor is appropriate for any contract with a term greater than three years. S&P calculates the amount of debt by multiplying the risk factor by the present value of fixed payments, discounted by 10 percent. This methodology is transparent and any changes to the S&P formula can be readily accommodated.

To balance the debt associated with the contract, the utility must inject equity in its capital structure to maintain the same debt/equity rations as before, which results in higher capital costs. This rebalancing of the capital structure is consistent with sound economics and the treatment afforded these obligations by other regulatory agencies. If these very real rebalancing costs are ignored, PPA and other contracted power supply is incorrectly evaluated and customers ultimately bear the costs, not the bidder. This is because the RFP evaluation process endeavors to locate the best deal for customers by determining the overall

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revenue requirement impact. Moreover, any comparison of bids that do not include these rebalancing costs would be skewed because they would not be based on a level playing field.

Some parties believe that if imputed debt is to be taken into account, then the independent evaluator ("IE") should be empowered to evaluate the impact of direct debt for a utility-owned resource, BOT or EPC, on the utility's capital structure and costs so that the two resources may be evaluated comparably. (See NIPPC Opening Comments at 11; ICNU Opening Comments at 9.) PacifiCorp believes that the impact of debt upon utility owned alternatives has already been taken into account within its current evaluation methodology as demonstrated in the Company's filing in UM 1208 and therefore believes this issue is appropriate for an IE to opine on during the RFP process. In contrast, PacifiCorp does not believe that it is reasonable to say that, because there may be a missing part in the equation, the entire math problem should be scrapped as appears to be proposed in the Joint Opening Comments (e.g., to only discuss imputed debt in the IRP process not in the RFP process). (Joint Opening Comments at 4-5.) The parties to this docket are not arguing that imputed debt costs are not real costs. Consequently, it is a much more reasonable approach to ensure fair treatment but full consideration of known costs, *e.g.*, to consider the impact on the capital structure for both PPAs and utility-owned options, and then to ignore this real cost altogether in the RFP process.

D. Multi-State Utilities

PacifiCorp agrees with Idaho Power Company's concern that changes to Order 91-1383 not be implemented to create rigid requirements that may not be compatible with procedures followed in other states. (*See* Idaho Power Company's Opening Comments at 6-7.) The Commission should maintain the flexibility for multi-state utilities to demonstrate compliance with the concepts of the guidelines without technical compliance if other states have differing requirements and/or permit a utility request for a waiver.

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III. CONCLUSION

In Order 91-1383, the Commission established competitive bidding requirements for investor-owned electric utility companies that struck the appropriate balance between making the bid evaluation process understandable and fair, and the need to make the process as flexible as possible. PacifiCorp continues to urge the Commission to retain the durability and flexibility in that approach and to reject recommendations to set prescriptive guidelines that increase risk to ratepayers and that cannot weather changes in circumstance, advancing technologies, and evolving energy markets.

DATED: October 21, 2005.

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CERTIFICATE OF SERVICE

I hereby certify that I served the foregoing document upon the parties of record in Docket UM 1182 on the date indicated below by mailing a true copy to said person(s), at his or her last-known address(es) indicated below.

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BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON

UM 1182

In the Matter of an Investigation Regarding Competitive Bidding	**PACIFICORP'S REPLY COMMENTS**

PacifiCorp hereby respectfully submits its reply comments. Responses specific to the opening comments of the Oregon Public Utility Commission (the "Commission") Staff ("Staff") are in Section I and responses specific to the opening comments of other parties to this docket are in Section II.

I. RESPONSE TO STAFF'S COMMENTS

A. Guideline 2: RFP Requirement

In its Opening Comments at 3, Staff explains that it arrived at its greater than 5-year and greater than 50-MW Major Resource definition by reviewing the energy risk management policies of Oregon's investor-owned electric utilities. According to Staff, this review showed that transactions with delivery terms greater than 48 months generally require prior approval by senior management. *Id*. It follows, Staff reasoned, that duration must therefore define a "significant energy resource". *Id*. Staff has since explained to PacifiCorp (in an October 14, 2005 telephone conversation) that Staff is currently evaluating whether to increase the quantities trigger to 100 MW in its Reply Comments. PacifiCorp notes that other parties' comments, including the joint opening comments of the Citizens' Utility Board, Renewable Northwest Project and Northwest Energy Coalition ("Joint Opening Comments") and the opening comments of Portland General Electric, also suggest changing Staff's major resource definition to increase the size to 100 MW. PacifiCorp agrees.

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As explained in more detail in PacifiCorp's Opening Comments at 3-4, a low threshold, such as 5 years and 50 MW, will likely result in higher costs and risk for ratepayers, because such a low threshold establishes a bias towards short-term power purchase agreements ("PPAs") and potentially no development of new assets, and will impair PacifiCorp's ability to actively hedge its position in the liquid forward markets. Moreover, because PacifiCorp operates a 9,000 MW system, a 50 MW resource does not represent a significant resource. Therefore, PacifiCorp urges the Commission to increase the major resource size definition from 50 MW to 100 MW.

In addition, as already set out in its opening comments, PacifiCorp urges the Commission to define the duration portion of the definition as 10 years, rather than Staff's proposed 5 years. PacifiCorp understands Staff's difficulties in deciding how best to define a significant resource, and appreciates Staff's willingness to reconsider the quantities requirement. However, PacifiCorp believes that Staff's underlying reasoning with respect to the proposed 5-year duration is incorrect because Commission-established RFP parameters should not be tied to corporate risk management policies that are subject to change. Corporate risk management policies are internal operational documents that change from time to time depending on factors not necessarily tied to whether or not a transaction involves a significant energy resource. Such factors influencing risk polices may include a utility's risk tolerance which will vary through time as internal and external conditions such as market conditions, capital and cash allocation and counter-party credit requirements vary. These factors do not necessarily depend on the resource being acquired but can vary depending on the individual utility, the type of counter-party (legal structure) and the structure and nature of the specific transactions.

Rather than looking to utility specific documents that can vary over time, PacifiCorp recommends that the Commission look to the IRP because the IRP identifies, in a public setting, significant resources as part of its planning process. Moreover, the Commission and

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other parties have consistently taken the position that the IRP and any resulting RFP process should be better aligned. If the Commission were to approve Staff's 5 year trigger for the RFP, the Commission would create exactly the opposite result, *i.e.* inconsistencies and disconnect, because PacifiCorp's IRP uses a 20-year planning horizon with an Action Plan for the next 10 years.

PacifiCorp's IRP specifically targets long-term supply side resource additions (10 years or more) to meet future needs. It follows that RFPs issued for long-term resources should focus on time horizons that are consistent with those studied in the IRP. The horizons for long-term IRP proxy (significant) resources studied in the IRP are not 5 years as evidenced by Appendix C (Table C.27) to PacifiCorp's most recently filed IRP. In fact, the supply side resource alternative with the shortest design life is 10 years (in the case of customer owned standby generation); most are supply side alternatives of 20 years or more. To the extent that the resource is not identified as a significant resource in the IRP, and as part of the development of an Action Plan, then the utility would consider the length or deficit on the system to be a balancing activity that should not be constrained by a formal and lengthy process intended to address long-term resource additions. The market for significant resources (long-term resources) clearly desires a reasonably transparent process to understand what the utility will use as its benchmark. Indeed, this is a key theme expressed by parties to this docket and PacifiCorp agrees.

Consequently, PacifiCorp proposes that resource and planning horizons should define what constitutes a significant resource in an RFP just like it does in an IRP. PacifiCorp encourages the Commission to align the IRP and the RFP by looking at a term consistent with the long-term planning horizon studied in the IRP.

Moreover, such an approach is consistent with the liquid forward markets available to utilities. (*See* PacifiCorp Opening Comments at 3-4.) These market opportunities do not fit well with lengthy competitive bidding processes and therefore, if a 5-year RFP trigger is

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mandated, may result in these opportunities being lost to utilities. If these opportunities are lost, then the price risk associated with balancing PacifiCorp's system will increase. As a result, the risk that the cost to ratepayers would be higher would increase as well. No party to this docket has expressed a desire to have an ineffective procurement process for long-term resources. PacifiCorp encourages transparency and will define a benchmark as a means to ensure competitive behavior in the market.

Staff's proposal may also create a bias against resource alternatives based on new assets, either build or purchase agreements from new assets. Bidders have indicated in the past that new asset backed resources are difficult to finance unless some portion of the output is committed for the long term. Entities who are willing to construct new assets indicate a desire for purchase agreements from those facilities with terms greater than 10 years. Consequently, Staff's position would lead to a bias towards PPAs and limit the RFP process and its participation to either power marketers with no assets or wholesale qualified entities with existing assets. Ultimately, this may lead to an increase in costs to utilities and its ratepayers, by artificially restricting the market alternatives because it sets up a scenario where power purchase and new asset build, cannot compete against one another. Therefore, the Commission should establish a process that allows PacifiCorp, and consequently ratepayers, to fully benefit from market opportunities and a level playing field between PPA and asset-backed resources.

B. Guideline 3: Exceptions to the RFP Requirement

It is PacifiCorp's understanding (based on its conversation with Mr. Galbraith) that Staff's RFP exceptions contemplate a process whereby a utility seeking to pursue a resource in the case of an emergency or market opportunity (not involving a self-build or owned option) completes the transaction without prior Commission approval, and that the prudence of such a transaction will be evaluated in the next rate case. A waiver, on the other hand, would only be used when a utility wishes to proceed without an RFP due to requirements or

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circumstances specific to the resource (for example, a joint project with other utilities to build a plant that uses coal as fuel). PacifiCorp understands that Staff is considering removing the "self-build resources" carve-out in the exception guideline; if that is the case, PacifiCorp has no objection to this Guideline.

Alternatively, a waiver process (without any exceptions for major resources), with an opportunity for expedited process where necessary, may also be a reasonable compromise of the parties' positions in this proceeding. PacifiCorp does, however, strongly object to the prohibition on using the exception process for self-build resources for the reasons stated in its opening comments.

C. Guidelines 8(a) and 12: Utility Benchmark

In its Opening Comments at 5, Staff states that "Staff recommends that selection of an initial short-list of bids be based on price and non-price factors," and that "[t]he non-price score [should] be based on the resource characteristics identified in the utility's IRP Action Plan (e.g., resource duration, dispatch flexibility, portfolio diversity, etc.) and conformance to the standard form contracts attached to the RFP." This language applies to the utility's benchmark via Guideline 12. While Staff does not appear to view the utility benchmark as a bid, Staff apparently does believe that the utility benchmark should be evaluated consistent with bidders using price and non-price factors.

As a general matter, PacifiCorp agrees that any benchmark option is not the same as a bid. That fact should reasonably lead to the conclusion that a utility benchmark option should not be treated the same as a bid. The purpose of the benchmark option is to offer a hedge against the market to protect the utility, and consequently ratepayers. Absent new information being available since the IRP is published, the proxy resource in the IRP will typically be used to identify the benchmark option and resource characteristics identified in

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the utility's IRP Action Plan[1]. The benchmark, by definition, always gets a full score on non-price factors (not price factors) because it is consistent with the minimum requirements identified in the RFP. Such minimum requirements typical relate directly back to the proxy resource identified in the IRP. For that reason, PacifiCorp questions the value of evaluating a benchmark on non-price factors.

If, however, parties intend to expand the scope of the non-price criteria beyond those criteria previously included in recent RFPs to include factors such as construction cost overrun risk, PacifiCorp must oppose any such proposal. (*See, e.g.,* Northwest Independent Power Producers Coalition ("NIPPC") Opening Comments, Attachment A, Guideline 5(f)).

The benchmark option is a cost-based alternative provided by the utility for the protection of ratepayers and pursuant to the then-current regulatory compact. Under the current regulatory scheme, such options may be evaluated at cost.[2] Under that scenario, PacifiCorp is permitted to earn no more than its authorized rate of return set in comparison to comparable utilities. Likewise, while ratepayers may pay additional costs for the project (if deemed prudent), they will also get the benefit if the utility achieves any cost savings, which savings are generally, not shared with the utility in PPAs. These rules establish a very different economic paradigm than exists for bidders who may offer to take certain types of

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[1] PacifiCorp notes that Staff's example resource characteristics identified in the Action Plan include "resource duration." For all of the reasons previously discussed in PacifiCorp's filings in this docket and in UM 1056, PacifiCorp strongly opposes a requirement to model resource duration in the IRP as impractical and unworkable in advance of knowing what the market will offer. Without repeating all of those comments here, PacifiCorp wishes to direct the Commission to those comments for PacifiCorp's opinion on the issue.

[2] In Order 05-133 in Docket UM 1066, the Commission directed the parties to focus on cost, not market, in proceeding through the investigation under UM 1056. The Commission also held that until the resolution of UM 1066, utilities must file a request for a waiver of the administrative rule when the utility wishes to include a new resource in its revenue requirement at cost, not market. While the order did not explicitly direct parties in UM 1182 to focus on cost, not market, until there is further direction in UM 1066, the cost/market issue is also implicated in this proceeding as it is unclear how the market rule will operate and how, if it all, it would change the return on equity issue discussed above. Accordingly, PacifiCorp's comments are directed at the cost issue.

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risks and therefore, also expect to get much larger returns. If the Commission were to establish a scenario where the benchmark option were to be treated and evaluated like a "bid" (*e.g.*, where cost over or under runs and other similar non-price variables were considered in the first round evaluation), it would create a mismatch between the purpose of the benchmark option, the regulatory paradigm governing that option and the risk profile of the utility in comparison to bidders. Until the regulatory paradigm permits the utility to submit a "bid" on truly the same basis as other bidders, and thus recover greater than its allowed return on equity and/or operational income that exceeds its cost, the utility's cost-based alternative should not be treated the same as a "bid" in the evaluation of such non-price factors.

D. Guideline 8(b): Individual v. Portfolio Analysis

Staff recommends in its Opening Comments at 6 that "selection of the final short-list of bids be based on total system portfolio analysis using the utility's production cost and risk models to identify the best combination of resource additions." It is not entirely clear what type of analysis Staff is proposing in this language. If Staff is proposing that the utility conduct production cost modeling using the same assumptions from its most recent IRP in the selection of the final short-list, PacifiCorp agrees with the proposed language and indeed, in PacifiCorp's Draft 2009 RFP (Docket UM 1208), the Company has included a proposal to conduct this type of analysis.

PacifiCorp does not agree that it is appropriate, however, to redo the analysis of those assumptions in the RFP process. The time for the analysis and public input is in the long-standing and well-defined IRP process which takes place every two years with an update filing provided annually. Further, PacifiCorp does not understand the benefit of duplicating that analysis in two places, which may serve to increase costs to ratepayers or delay the process, with the ultimate result of the process not being successful. For example, some bidders are unwilling to leave bids open for a long period of time without building in a market movement premium or will likely refuse to enter into contracts if the market moves

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against them. As Staff has itself acknowledged, rerunning the IRP modeling, by reconstructing the portfolios, is an exercise in judgment that balances costs and risk—which takes time. The extended evaluation time could result in the utility losing best-price bids, as well as extending the RFP process to unmanageable lengths of time. Instead, the RFP process must tie to the IRP, and it does under the Company's proposal; however, the RFP process should also be a flexible and nimble process that is not overly cumbersome and costly, or does not create barriers to entry by the market.

Finally, if it is Staff's position that a portfolio analysis must include analysis of uneconomic bids, PacifiCorp opposes that proposal for the reasons stated in its Opening Comments. Put simply, the Company will seek to acquire the resources identified in the Action Plan, including those identified as providing value to the portfolio in terms of adding diverse resource options, such as the renewable target. It may do so in the context of single-source RFPs. It would not be appropriate however to require the utility to conduct all-source RFPs for the sole purpose of "adding" otherwise uneconomic bids together with economic bids to achieve the diversity target. Moreover, even if the resources together may be economic, such an approach creates significant practical hurdles in addition to potential prudence challenges in trying to negotiate with two (or more) bidders at the same time in order to achieve the portfolio outcome. If the economic bidder drops out of the process for whatever reason, PacifiCorp would be left with only the uneconomic bid. PacifiCorp believes that the regulatory process in this and its other states will not permit the Company to acquire uneconomic resources without creating serious prudence challenges. Finally, such a proposal might serve as an impediment to the market by not providing a clear signal of what it takes to win the RFP. As recent Federal Energy Regulatory Commission proceedings have made clear, ambiguity in RFPs can serve to chill participation.

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II. COMMENT IN RESPONSE TO OTHER PARTIES' COMMENTS

A. NIPPC Guideline 5: "Benchmark Option"[3]

NIPPC has proposed that the IE "will score all bids separately" from the utility. In contrast, Staff's guideline covering this topic (Guideline 13(b)(ii)) states that the IE will validate the Benchmark Score and "may validate, sample, or independently score all bids, at the discretion of the IE and the Commission." Staff's approach is a more reasonable approach in the RFP context. The IE, at the Commission's direction, should score as many bids as the IE believes are necessary for the IE to be able to reach a professional judgment that the process was fair and the result was reasonable. Based on actual experience, where bidders submit more than one bid changing only a few criteria, it may be possible that the IE, exercising its professional judgment will determine that it is not necessary to score a similar bid because the IE can tell that the bid is not as economic as the other options from that bidder. While PacifiCorp would not object to an IE scoring all bids if that IE believed such a step was necessary, PacifiCorp does not believe the requirement that the IE must score all bids is reasonable or necessary and can only serve to increase the cost to bidders and ratepayers for IE services.

B. Guideline 6: Utility Ownership Options

Both the opening comments of the NIPPC and the Joint Opening Comments propose that Oregon's competitive bidding guidelines should explicitly state that bidders may submit a bid to construct at the utility's site. (*See* Joint Opening Comments Attachment at 2; NIPPC Opening Comments at 12.) PacifiCorp opposes the imposition of such a requirement in all RFPs.

As an initial matter, it is important to point out that it is PacifiCorp's intent to offer its site to bidders when it has a site that is already partially developed and paid for by ratepayers,

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[3] NIPPC's Attachment A uses a different numbering scheme that does not correlate to Staff's Proposed Guidelines.

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and when the bidder is bidding to a specific bid specification which can be adequately outlined in the RFP. To the extent that the utility will own and operate the asset that is the result of an engineering, procurement and construction ("EPC") bid or a build-own-transfer ("BOT") bid, it must be consistent with the specifications of the reference plant in the RFP. It may be appropriate under those circumstances, as suggested by NIPPC, to permit EPC bids or BOT bids. For example, such options are available under RFP 2009 as drafted. However, it simply is not reasonable or prudent to force a utility to own and/or operate any asset that a bidder may choose to offer. This is not in the best interest of customers or the utility and creates risk increasing and overly proscriptive and inappropriate requirement to include in the guidelines.

First, if such a requirement is considered it should be limited to the type of risk the utility should be willing to take at the particular site. EPC and BOT bids provide different risk profiles for the utility, and ultimately, ratepayers. In both cases the utility will be required to own and operate the facility however, the development risks associated with each of them are different. Under an EPC bid, the bidder takes the construction risk, but typically leaves the development risk with the utility. Under a BOT bid, the developer typically takes both the development and construction risk. It is possible that PacifiCorp's analysis may show that it is not a good option for ratepayers to be required to take the development risk at a certain site depending on the site-specific characteristics. There are many variables that must be taken into account when considering if bidders should be allowed to bid the utility's site. Key amongst these are site-specific risks (such as development) and resource-specific operational or infrastructure criteria. A requirement that the utility always permit EPC bids on its site could easily result in ratepayers being inappropriately exposed to risks that cannot effectively be managed or hedged (risks including but not limited to environmental, water availability, permitting and wetland issues).

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Moreover, a utility-developed site may provide best value to ratepayers if it is utilized to its fullest potential (then or in the future). A utility develops its sites with a certain size of resource in mind taking into account water availability, air permit restrictions, fuel, and other critical development issues such as potential future use. If a site could be developed to accommodate a large project (*e.g.* 500 MWs or more), the value of the site will be diluted for ratepayers if there are no restrictions on the size of the project a bidder can offer to build on the site. Also, if the resources at the utilities sites are each different then, integration, operation, maintenance and interconnection may become a problem.

Similarly, if the utility is accepting BOT and EPC options at the utility site (as well as PPA options), it is important that the bidders build to the engineering specifications provided by the utility. If not, the utility cannot reasonably expect to acquire a plant at the end of the process that can operate in a manner that is best integrated with the utility's system. For example, PacifiCorp may specify in engineering specifications that certain types and standards of equipment be used in the construction process. Such a requirement offers value to ratepayers because the utility may have the same type of equipment at other sites which it can physically utilize in emergencies or its crews may be better trained to maintain and/or repair. Also, in these situations, it is the utility and ratepayers, not the EPC or BOT bidder, who has the long-term commitment to the plant and therefore, specifications and quality, are critically important. Such a requirement also provides benefits to bidders as it provides a high degree of transparency, allows bidders to be compared on the merits of their competitiveness (rather than potentially undesirable design alternatives), and provides customers with the further benefit of having such bids compared from a common set of specifications.

The magnitude of these issues and costs are greatly increased when fuel-type is taken into consideration. For example, for a coal plant benchmark option, the timeline is longer

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and the cost and complexity is greater for permitting and specifications related to the utility site.

Finally, PacifiCorp may not have a site to include, for example in the most recent renewable resource RFP. Therefore, if this were to be made a requirement, it should be limited to situations where a site is available for use.

The proposed guideline fails to take any of these variables into account requiring instead just a blank offering of the utility site without any cautionary restrictions. It would provide more value to ratepayers to consider these options on an RFP by RFP basis. Therefore, PacifiCorp believes that a far better approach to this proposed issue is to leave the consideration of whether to permit bidding on the utility site to the review of the draft RFP. The utility could include an explanation with its filing explaining why it chose to include or not include such an option. To the extent a potential bidder has a strong value proposition for customers, the potential bidder is afforded the opportunity to comment during the public comment period.

C. Guideline 8(c): Debt Imputation

Some parties have taken issue with the way in which Staff proposes to use imputed debt as an evaluation criterion. (*See* NIPPC Opening Comments at 10-12; Industrial Customers of Northwest Utilities ("ICNU") Opening Comments at 9-10; Joint Opening Comments at 4-5.) PacifiCorp assumes that there is no dispute regarding direct debt (*e.g.*, debt directly applied on PacifiCorp's financial books as a result of accounting standards), because all parties who commented on the issue are focused only on imputed debt. This lack of comment on direct debt is unremarkable given that the thrust of the parties' comments is a question of subjectivity with respect to imputed debt that cannot reasonably be argued to even exist with respect to direct debt. Accordingly, PacifiCorp requests that the Commission recognize the consideration of direct debt on any bid that results in such an accounting designation.

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With respect to imputed debt, as already explained in PacifiCorp's Opening Comments at 9-10, imputed debt can impose a very real cost on ratepayers that should be factored, consistent with the application of the cost of direct debt, as part of the first round of the resource evaluation process. Imputed (also referred to as "inferred") debt results when credit rating agencies infer an amount of debt associated with a power supply contract (inclusive of PPAs) and take the added debt into account when reviewing the utility's credit standing. This is due to the fact that the fixed charges associated with power supply contracts increase the utility's financial risk in the same way that long-term debt and other financial obligations increase financial risk. Consequently, investors, as well as regulators and the accounting profession, regard the fixed obligations associated with such contracts as being equivalent to debt.

There are readily identifiable and verifiable methods of calculating the imputed debt associated with PPAs and other contracts. Standard & Poor's Corporation ("S&P"), for instance, has determined specifically for PacifiCorp that a 50 percent risk factor is appropriate for any contract with a term greater than three years. S&P calculates the amount of debt by multiplying the risk factor by the present value of fixed payments, discounted by 10 percent. This methodology is transparent and any changes to the S&P formula can be readily accommodated.

To balance the debt associated with the contract, the utility must inject equity in its capital structure to maintain the same debt/equity rations as before, which results in higher capital costs. This rebalancing of the capital structure is consistent with sound economics and the treatment afforded these obligations by other regulatory agencies. If these very real rebalancing costs are ignored, PPA and other contracted power supply is incorrectly evaluated and customers ultimately bear the costs, not the bidder. This is because the RFP evaluation process endeavors to locate the best deal for customers by determining the overall

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revenue requirement impact. Moreover, any comparison of bids that do not include these rebalancing costs would be skewed because they would not be based on a level playing field.

Some parties believe that if imputed debt is to be taken into account, then the independent evaluator ("IE") should be empowered to evaluate the impact of direct debt for a utility-owned resource, BOT or EPC, on the utility's capital structure and costs so that the two resources may be evaluated comparably. (See NIPPC Opening Comments at 11; ICNU Opening Comments at 9.) PacifiCorp believes that the impact of debt upon utility owned alternatives has already been taken into account within its current evaluation methodology as demonstrated in the Company's filing in UM 1208 and therefore believes this issue is appropriate for an IE to opine on during the RFP process. In contrast, PacifiCorp does not believe that it is reasonable to say that, because there may be a missing part in the equation, the entire math problem should be scrapped as appears to be proposed in the Joint Opening Comments (e.g., to only discuss imputed debt in the IRP process not in the RFP process). (Joint Opening Comments at 4-5.) The parties to this docket are not arguing that imputed debt costs are not real costs. Consequently, it is a much more reasonable approach to ensure fair treatment but full consideration of known costs, *e.g.*, to consider the impact on the capital structure for both PPAs and utility-owned options, and then to ignore this real cost altogether in the RFP process.

D. Multi-State Utilities

PacifiCorp agrees with Idaho Power Company's concern that changes to Order 91-1383 not be implemented to create rigid requirements that may not be compatible with procedures followed in other states. (*See* Idaho Power Company's Opening Comments at 6-7.) The Commission should maintain the flexibility for multi-state utilities to demonstrate compliance with the concepts of the guidelines without technical compliance if other states have differing requirements and/or permit a utility request for a waiver.

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III. CONCLUSION

In Order 91-1383, the Commission established competitive bidding requirements for investor-owned electric utility companies that struck the appropriate balance between making the bid evaluation process understandable and fair, and the need to make the process as flexible as possible. PacifiCorp continues to urge the Commission to retain the durability and flexibility in that approach and to reject recommendations to set prescriptive guidelines that increase risk to ratepayers and that cannot weather changes in circumstance, advancing technologies, and evolving energy markets.

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