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August 25, 2008

Traci Kirkpatrick
Administrative Law Judge
Public Utility Commission of Oregon
550 Capitol St NE – Suite 215
PO Box 2148
Salem OR 97308-2148

Re: UM 1368 – Comments from the Oregon Independent Evaluators
Boston Pacific Company

Dear Judge Kirkpatrick:

Enclosed with this letter is a document entitled "Supplemental Comments of the Independent Evaluator" that staff is submitting in PUC Docket UM 1368 on behalf of one of the Oregon Independent Evaluators, Boston Pacific Company.

The attached document is a public document that contains no confidential information. Please note that I am serving this document on the other UM 1368 parties via email only.

Sincerely,

Michael T. Weirich
Assistant Attorney General
Regulated Utility & Business Section

MTW:nal/#933896
Enclosure
cc: All parties by email only w/enc.

MEMORANDUM

August 22, 2008

TO: Lisa Schwartz
Oregon PUC

FROM: Craig Roach
Frank Mossburg
Andrew Gisslequist

SUBJECT: Supplemental Comments of the Independent Evaluator

The purpose of this memo is for the Oregon Independent Evaluator (IE) to provide additional comments in response to PacifiCorp's revised draft 2008R-1 RFP as filed on July 28, 2008, and related commentary. We break our comments down into several sections based on key issues; (a) Mandatory Asset Purchase Option, (b) Production Tax Credit, (c) Capacity Value, (d) Right to Purchase Equipment, and (e) Other Issues.

ISSUE-BY-ISSUE COMMENTS

Mandatory Asset Purchase Option

PacifiCorp continues to request that all bidders who offer a Power Purchase Agreement (PPA) must include a clause that grants the Company a purchase option for the facility in question at the end of the contract term. While PacifiCorp set the purchase option amount at $1 in its initial draft filing they have since altered the draft PPA to allow the bidder to specify the price to be paid for the asset at the end of the contract term.

The IE continues to believe that requiring a purchase option is not in the best interest of Oregon ratepayers and will only serve to raise prices to ratepayers and reduce competition. This could happen in at least four ways.

- First, the mandatory offer requirement will directly increase bid prices. The bidder will have to be compensated for relinquishing their asset after the contract has ended. The bidder will either increase their contract price or ask for a high price for the forced asset sale at the end of the contract. As a result, the ratepayers pay more for a contract than they otherwise would or the purchase

decision is changed to an offer that would be more expensive absent the asset sale requirement.

- Second, the mandatory offer requirement could increase costs to ratepayers by preventing quality competitors from offering into the RFP in the first place. A bidder with a quality asset now must give up that asset if they wish to participate in this RFP. Given this choice, bidders may elect not to participate at all, and thus deprive ratepayers of quality offers (and lower prices).

- Third, the mandatory offer requirement could hurt future competition by removing players from the market. Any winners from this RFP will be forced to give up their assets to PacifiCorp. Thus, future RFPs will have fewer competitors, fewer quality choices, and possibly higher prices, for ratepayers.

- Fourth, given that this is envisioned to be an RFP that will be reissued as the Company sees fit to fulfill future needs, a mandatory offer requirement could discourage future competitors from developing renewable assets in the market. No bidder with an interest in developing a continuing, long-term, operating portfolio will want to develop projects in PacifiCorp's territory, knowing that they will only have to turn those over to the Company at some point or another. Again, this could raise future costs to ratepayers by depriving them of quality choices and lower prices.

The only potential benefit to the mandatory asset purchase option is that ratepayers might get a good deal on a renewable asset site twenty to twenty five years from now.[1] That is, a bidder could guess wrong and offer an asset price that is lower than the actual asset value in the future. In our view, this speculative benefit does not outweigh the above drawbacks and the measure is likely to simply lead to increased costs for ratepayers in the near term.

Because of its chilling effect on competition and thus, the resulting increase in prices, mandatory asset purchase options are not common. They are not in PacifiCorp's major supply side RFPs and they are not in renewables RFPs from producers such as Duke Energy Ohio, SWEPCO, PNM and APS.

A solution that has been mentioned is to remove the mandatory nature of the purchase option clause for PPAs and, instead, assign some end-of-life or

[1] Twenty years is the Company's 2007 IRP estimate of a wind project's life span.

salvage value benefit to BOTs and Benchmark bids. While this solution is somewhat of an improvement, it still has problems. While we agree that there is some end-of-life or salvage value to a renewable asset (typically from the site) it is extremely difficult to state this value with any certainty twenty years ahead of time. This is particularly true when the asset value is so dependent on legislation (such as the Production Tax Credit and Carbon Emissions legislation) to drive value. PacifiCorp states that the value is "substantial" but we again note that their original offer price was $1. Furthermore, as Renewable Northwest Project (RNP) notes in their comments, site values are different depending on the nature of the permitting and lease agreements in the proposal.

The danger with this proposal is that it could improperly tilt the selection decision. If evaluators attach a significant salvage value to BOTs and Benchmarks we could end up selecting an asset that is *more* expensive over a twenty or twenty-five year period in the hope that we "guessed right" and that salvage values really are high. Because of this difficulty we think that the salvage value of BOTs and Benchmarks should only have a "tiebreaker" effect on the asset purchase decision. PPA bidders would, of course, be free to offer asset purchase options if the wished, but these too would only have a "tiebreaker" effect.

In conclusion, rather than include a clause which will cause higher prices and competitive harm, or try to accurately value an asset twenty years from now, a far simpler way to benefit customers is to hold a competitive RFP which invites a wide range of bidders, and simply pick the bid which offers the best deal for the specified contract term. This assures that ratepayers will get the best deal, allows competition to grow, and increases the chances of quality offers in the future.

Production Tax Credit

PacifiCorp continues to request that PPA bidders be solely responsible for any change in the status of the Production Tax Credit (PTC). They claim that this requirement places the bidder in a "symmetrical" position with the Company, apparently because the Company can only recover incurred costs.

As noted in our original RFP Design Report, the great strength of contracts is that they allocate risks to those parties who are best equipped to manage that risk. The risk of PTC extension is not within the control of bidders so it makes no sense to ask them to manage that risk when they can do nothing about it. For this reason renewables RFPs often make some allowance for changes in the PTC.

Furthermore, we completely fail to see how forcing a bidder to take the risk of PTC extension puts it in a "symmetrical" position to the Company. In fact,

it places the PPA bidder at a detrimental position to BOT bidders and Company Benchmarks, which can simply pass this risk on to ratepayers. Allowing bidders to specify a "with and without" PTC price (as we have suggested) would, in fact, be the way to make symmetrical positions, as well as assure transparency and place PPA bids on equal footing with Benchmarks and BOT bids. This would have the added benefit of allowing those bidders who *are* willing to take on some risk to do so and thus, provide an advantageous bid.

Given that we are allowing "with and without" pricing it makes sense that PacifiCorp should also be required to analyze the performance of bids on a "with and without" basis. This would also seem to be proper, given that the PTC has yet to be extended and would also reveal the benefits of any PPA that wished to assume PTC risk by offering a low price in the "without" scenario.

Capacity Value

Staff and the IE have raised concern that the proposed ACC method does not take into account capacity values. In our RFP Design report we suggested that PacifiCorp devise some method for valuing capacity for this RFP. This would yield two benefits (a) it would give more benefit to resources such as geothermal or biomass facilities and (b) it would create a more complete account of the value for all resources.

We welcome any method that the Company wishes to propose. For our part, in order to assist in this effort we would make the following suggestion. First, PacifiCorp could assign a capacity amount to all resources based upon the methods used in the 2007 IRP. For wind resources, this would include a value based on location, as laid out in Appendix J of the 2007 IRP. Second, convert this capacity amount into a dollar value by multiplying the amount times the annual carrying cost for a new combustion turbine. This value, too, could come from the IRP, so as to be as transparent as possible. This calculation could be added into the ACC model for each month, discounted back to the present day, and divided by the net MWh, just like all other costs and benefits.

We note that the Company appears to think that this method has no analytical evidence to support it. Again, we welcome other proposals from the Company, however, we would note that the carrying cost of a new combustion turbine is a common measure for the value of new capacity, representing as it does the cheapest source of new capacity available to a market. For example, this cost is often used to set the maximum level of price offers in market mitigation situations, on the theory that prices should at least be able to rise to a level that attracts new investment in a market.

Right to Purchase Equipment

In our RFP Design report we requested clarification on PacifiCorp's requirement that a bidder show a right or an option to purchase turbines or other long lead-time equipment; in this context we also requested comments from interveners. RNP stated that, to them, the definition of an option was not a concern, so long as PacifiCorp was held to the same standards. PacifiCorp now states in the RFP that bidders must have a "contract to purchase major equipment (i.e. wind turbines) and a process to adequately acquire other critical long lead time equipment." PacifiCorp further claims that its Benchmark bids should not be held to the same standards as other bidders since these bidders are large developers and the Company has "fewer viable alternatives" for the sale of equipment should it not win the RFP.

While we agree that some bidders may have a larger array of options for turbine use than the Company we don't believe that all bidders are necessarily so advantaged. Given the active market for wind turbines we don't think that holding PacifiCorp to the same standards as a bidder places an undue risk burden on the Company. Moreover, if bidders have a true competitive advantage due to the bidder's broader involvement in wind generation, that should not be a factor that gets blunted by PacifiCorp.

If the Company is truly worried about this risk, we would suggest that it eases it's definition of "option" to one which the Company can live up to. Alternatively, as we mentioned and Staff re-iterates, the Company could accept site-only bids and use their turbines for these sites.

Other Issues

In addition to these four major issues, there are several other issues that we take note of. Other comments are presented in bullet-point form below.

- We note that the Company has not commented in depth on some of our major proposals, chiefly, for (a) what to do if the ACC method results in the Company not taking it's full 500 MW of need and (b) risk-adjusting the Company Benchmarks to account for their cost-plus prices as compared to the fixed prices of the bidders. The Company only states that it will not "change the two-step evaluation process" and may issue further RFPs as needed. The Company has not stated why it should ignore the CO_2 emissions costs levels from the IRP or the potential value of RECs generated by renewable assets should it choose not to take the full 500 MW. Nor does it state why Benchmark bids should not be assessed some

sort of penalty for their cost plus nature, which causes higher risks for ratepayers. We continue to hold to our recommendations laid out in our RFP Design Report.

- Staff asks for comment on the level of success fee proposed by PacifiCorp. A potential one million dollar success fee may not be very much in the context of the overall bid cost. For example, a 100 MW wind project will likely have a capital cost of almost $200 million. However, it is very high compared to industry standard bid fees, and thus we fear it may deter bidders from participating. We again invite bidder comment on the issue.

- We believe the proposed non-price factors are generally sufficient; though we welcome bidder comments where definitions are unclear. As an additional measure, we would suggest that the metric "realism of net output projections" be included within the "operational viability" category. Since bidders will be estimating their generation, we think it is proper to have some way of penalizing bids which make unrealistic estimations.

- We have reviewed what we believe to be the draft asset purchase agreement. PacifiCorp did not provide the document in it's filing, but rather refers to an Appendix which points to a previously provided document entitled "Wind Development Asset Acquisition and Sale Agreement." This document was provided in the Company's initial filing and reviewed in our RFP Design Report. In general we find it to be satisfactory, through, as always, we welcome feedback from participants.

- The Company states that "Up to 500 MW" will be taken on each initial shortlist for the wind and non-wind categories of bids. We would suggest that the "ceiling" number be raised to 1,000 MW. The reason for this is that projects may be up to 300 MW in size. This could lead us, particularly in the wind category, with only two or three bids making it to the initial shortlist. This, in our opinion, would not be the sort of supplier diversity that is required on the initial shortlist. Note that this would not obligate the Company to take this much to the shortlist, if there are clear separations among projects they may take less.