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**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

UE 102

In the Matter of the Application of Portland)
General Electric Company for Approval of the) ORDER
Customer Choice Plan.)

**DISPOSITION: AUCTION PROCESS STIPULATION ADOPTED; PGE
AFFILIATES BARRED FROM PARTICIPATION IN THE AUCTION PROCESS**

Background

On December 1, 1997, Portland General Electric Company (PGE) filed rate schedules in Advice No. 97-20 to be effective January 7, 1998. The filing requested approval of PGE's Customer Choice Plan, which would introduce competition for the supply of electricity for all PGE customers and allow PGE to sell its supply portfolio. On January 6, 1998, the Public Utility Commission of Oregon (the Commission) issued Order No. 98-015 suspending the Advice.

On April 7, 1998, PGE filed a Supplemental Application for Approval of the Auction Process for the sale of PGE's supply portfolio. This Application requested approval of a two-stage, sealed bid auction process. On August 5, 1998, Administrative Law Judge Allen Scott granted a motion by PUC staff (Staff) to establish a separate schedule within this case for consideration of the issues dealing with the proposed auction process. On December 17, 1998, the Commission issued Order No. 98-534 denying PGE's motion to make the auction process generic, i.e., applicable to other Oregon electric utilities.

On January 27, 1999, the Commission issued Order No. 99-033 in this docket. The Order rejected in part PGE's Customer Choice proposal and set out the Commission's proposed plan to allow industrial and most commercial customers to buy electricity from competitive suppliers and to permit residential and small commercial customers to buy electricity at portfolio rates or cost of service rates. The Order recognized that the auction process would be considered in a separate order.

Following prehearing conferences and other prehearing procedures, a hearing was held on the auction process issues on June 8, 1999, in Salem, Oregon, before the Administrative Law Judge. Following the hearing, settlement conferences were held among the parties in June and July 1999.

The Stipulation

On July 26, 1999, PGE submitted a Stipulation to the Commission relating to the auction process. It was signed by PGE; Staff; the Citizens' Utility Board; and the City of Glendale, California (Stipulation Parties). On August 2, 1999, PacifiCorp filed a letter stating that it did not oppose the Stipulation but would not sign the Stipulation.

The Stipulation is an agreement among the signatory parties as to all issues relating to the auction process except whether an affiliate of PGE can participate in the auction. The Stipulation Parties agreed that all parties could file briefs relating to the affiliate issue in accord with a schedule approved by the Administrative Law Judge. Opening briefs were filed by PGE, Staff, and the City of Glendale. Reply briefs were filed by PGE, Staff, Chelan PUD, and the City of Glendale.

The Stipulation contains recitals of pertinent facts, a description of the auction process, stipulation procedures, and, in Attachment B, the auction protocols and procedures. It may be summarized as follows.

The auction is a two-step process, with both steps utilizing sealed bids. When PGE decides to sell some or all of its supply portfolio, it will give notice to the PUC. It then will conduct a solicitation and qualification process for bidders. The qualification process requires potential bidders to provide a summary of their operating experience in the energy industry and proof of their ability to close an acquisition transaction of the magnitude contemplated in the auction. A prospective bidder who is disqualified by PGE has a right to file a complaint with the Commission to challenge the denial and to continue to participate pending resolution of the complaint. The Stipulation also provides that PGE inform potential bidders that the Commission will conduct an independent study to determine if any bidder's purchase of the generation or contract assets involved in the auction would have an effect on competition in the relevant markets inconsistent with the public interest.

Following the solicitation and qualification process, the first (preliminary, non-binding) bidding round will occur. PGE will provide an information memorandum relating to the assets to each qualified bidder. Prospective bidders may conduct due diligence reviews with respect to the assets. Bidders will then be required to submit preliminary, non-binding proposals. The bidders may bid on whatever assets they wish to purchase but those wishing to purchase all generating assets as a package must submit a bid for each generating asset plus a premium for the entire package. Bidders for power contracts may bid on the individual contracts they desire or for the entire package of power contracts.

PGE will review the first round bids and from them select "short-listed" bidders who can go on to the second round of the auction. Unless the Commission approves a different number of short-listed bidders, PGE will select, at a minimum, the highest five bidders for each generating or contract asset and, at a minimum, the highest five bidders for the package of generating or contract assets. If the highest five bidders for each asset or each package include two or more affiliated bidders, PGE must select, at a minimum, the highest five non-affiliated bidders plus the qualified affiliates.

At the beginning of the second bidding round, PGE will provide the short-listed bidders with a draft asset purchase agreement and other agreements necessary to complete the transaction. Bidders may propose revisions to these agreements. PGE will then develop a final version of the agreements based upon the comments from the bidders and will include final agreements and bidding instructions to second round bidders in a request for proposals (RFP).

Bidders in the second round may conduct detailed due diligence reviews. Bidders will then submit binding sealed bids based strictly on price and any alternative conditions permitted by the RFP. PGE will evaluate the bids using the criterion that all assets in the auction will be sold singularly or in combinations to produce the highest overall evaluated price. If PGE receives one or more bids within five percent of the initial winning bid for any asset, PGE will allow additional due diligence reviews and

then conduct a simultaneous ascending auction among those bidders who submitted bids within the five-percent range for that asset.

At the conclusion of the process, PGE will apply for approval of the property transfer under ORS 757.480. If the Bonneville Power Administration (BPA) adopts rules that would reduce PGE's rights to BPA Power if the auction process adopted by the Stipulation is followed by PGE, the Stipulation Parties, at the request of any one of them, will negotiate to revise the Stipulation to avoid any such reduction of PGE's rights.

Commission Disposition

The Commission has examined the Stipulation, the comments provided in support, and the testimony and exhibits in the record relating to the auction process. Our consideration is guided, as it was in Order No. 99-033, by our mandate in ORS 756.040 to “represent the customers” of public utilities and the public generally in matters pertaining to public utilities, to protect them from “unjust and unreasonable exactions and practices” and to obtain for them adequate service “at fair and reasonable rates.”¹ We have also reviewed the Stipulation in relation to the Governor’s Principles discussed in Order No. 99-033.² We conclude that the auction process described in the Stipulation is in accord with those principles and statutes and should be adopted.

PGE Affiliate Participation

PGE's Position. PGE argues that its affiliates should be allowed to participate in the auction. PGE notes that Staff’s initial objection to affiliate participation was based upon Staff’s concern that PGE's original proposal would give the company substantial discretion which it could use to favor an affiliate. PGE argues that the auction process adopted in the Stipulation mitigates that problem by reducing the discretion given to PGE and by providing for review by the Commission of most of the steps in the process. These changes, according to PGE, make fear of favoritism by PGE no longer a realistic concern.

Specifically, PGE notes that its discretion under the Stipulation is reduced in the following ways: a potential bidder excluded under the initial qualification process can file a complaint with the Commission and continue to participate in the auction process while the complaint is pending; PGE makes no market power determinations in qualifying potential bidders; PGE has no discretion over asset packaging; PGE has limited discretion in selecting short-listed bidders and its decision is reviewable by the Commission; PGE will conduct a “price only” auction in the second round, thereby eliminating its discretion to subjectively evaluate separate terms and conditions; all data requests from the short-listed bidders and PGE's responses to them will be reduced to writing without attribution and distributed to all short-listed bidders; final bids will be evaluated under the criterion that all assets will be sold and the highest overall evaluated price obtained will win the auction; if PGE receives bids within five percent of the highest bids in the second round, PGE will conduct a simultaneous ascending auction on a price only basis to determine the winning bidder; and finally, under ORS 757.480, the Commission must give final approval to the property transfer. The Commission will thus have the opportunity to hear the comments of other bidders regarding the auction and decide whether the sale is in the public interest.

¹ ORS 756.040; *See also* ORS 757.020; 757.210; Order No. 99-033 at 6.

² *See* Order No. 99-033 at 6.

If the Commission determines that the auction process as set out in the Stipulation does not provide sufficient protection to allow PGE affiliates to participate, PGE offers an alternative procedure. Under this proposal, an affiliate would be allowed to participate, but the ongoing process would be reviewed by an independent advisor, who would report to the Commission. The specific proposal is as follows:

At the beginning of the auction process, at PGE's expense, the Commission will hire an independent advisor, reporting directly to the Commission, to be involved in the auction process. The independent advisor will review all communications between PGE or its Advisor³ and the bidders and all discretionary decisions of PGE and its Advisor during the process including, but not limited to decisions on qualifying bidders, evaluating first-round bids, evaluating bidder qualifications for the second round, and selecting second round bidders. Should the independent advisor feel there has been any inappropriate activity or communication, the independent advisor will have the right to temporarily suspend the auction process until direction from the Commission can be obtained based on the concerns of the independent advisor.

PGE argues that use of the independent advisor would "resolve any remaining problems about the fairness of the auction process with the participation of a PGE affiliate."

The Position of Staff and the City of Glendale. PUC Staff and the City of Glendale make similar arguments against participation of a PGE affiliate in the auction process. They argue that the auction process established in the Stipulation, although modified from PGE's original proposal, is still a two-step, sealed bid process which continues to allow significant discretion on the part of PGE. It could thus lead to self-dealing. Moreover, they point out that a sealed bid process, by its very nature, can cause suspicion of corruption even where none is present. Lack of faith in the fairness of the process could lead to a reduction in participation or to a dampening of bids.

Specifically, Staff and Glendale point out that the disqualification process for potential first round bidders gives great discretion to PGE. The complaint process, they aver, will not cure this problem because it may be viewed by disqualified bidders as too expensive or uncertain in outcome to be of practical use. Staff also argues that an affiliate would have superior knowledge of the assets and that the form of auction set out in the Stipulation would not correct that problem. Moreover, the RFP that PGE would issue prior to the second round could, in the view of these parties, be designed to favor the PGE affiliate. Staff and Glendale also argue that the potential for self-dealing between PGE and its affiliates after the auction is not eliminated by the modified auction process.

Staff argues that use of an independent adviser, as suggested by PGE, would not eliminate the problems described above. The adviser would inevitably have less knowledge than PGE and its affiliates about what terms and conditions would benefit the affiliate or PGE. Moreover, Staff points out that several of the potential problems it has noted, such as the information advantage a PGE affiliate may have, the perception of that advantage by potential bidders, and the possibility of preferential treatment of affiliates in related transactions subsequent to the auction are not mitigated by PGE's proposal. Staff suggests that if the Commission decides to allow affiliate participation, it reopen

³ The "Advisor" referred to here is the Advisor retained by PGE to assist the company in developing the auction process and administering the auction.

the record for development of a process that addresses the concerns Staff has raised.

Commission Disposition

The Commission will not allow PGE affiliates to participate in the auction. The plan we approve must serve the public interest. One test of that goal is whether the process proposed will obtain the highest prices for the assets. The public interest is also served if the process is fair in reality and in appearance and does not occasion disputes about procedure. We conclude that although the modified process set out in the Stipulation reduces the potential problems associated with affiliate participation, it does not eliminate them. On balance, we conclude that affiliate participation should not be allowed for the reasons set out below.

First, we note that PGE will continue to have discretion in many areas under the stipulated procedure. Detection of misuse of that discretion may not be possible in all instances. Moreover, an affiliate inevitably will have advantageous information available to it that is unavailable to the other participants. Also, it is clear that an affiliate might be dealing with PGE on different terms after a successful bid than would other participants. All of these reasons establish that it is unwise to allow an affiliate to participate under the form of auction agreed to in the Stipulation. That participation could result in reduced participation or reduced bidding, possible disputes about the handling of the auction that might not otherwise occur, and other problems that would not serve the public interest. We see nothing in the record which suggests that the public interest will be harmed by exclusion of PGE affiliates. We conclude that the applicable statutes and Governor's Principles require that we decline to permit PGE affiliates to participate in the auction in this form.

PGE's alternative suggestion for use of an independent advisor is thoughtful. We conclude, however, that it does not mitigate the problems discussed above to a sufficient degree to convince us to adopt it. We welcome additional attempts to create a process that serves both the public interest and that of the auction participants. If PGE seeks to modify the proposal to attempt to remove the concerns that we have, we will reopen the record in this matter to allow for additional information.

ORDER

IT IS ORDERED THAT:

1. The Stipulation attached to and made part of this order as Appendix A is adopted by the Commission.
2. PGE affiliates may not participate in the auction described in this order.

Made, entered, and effective _____.

Ron Eachus

Roger Hamilton

Chairman

Commissioner

Joan H. Smith

Commissioner

A party may request rehearing or reconsideration of this order pursuant to ORS 756.561. A request for rehearing or reconsideration must be filed with the Commission within 60 days of the date of service of this order. The request must comply with the requirements in OAR 860-014-0095. A copy of any such request must also be served on each party to the proceeding as provided by OAR 860-013-0070(2). A party may appeal this order to a court pursuant to applicable law.

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