BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UM 1129

In the Matter of the	)	
	)	
PUBLIC UTILITY COMMISSION OF OREGON	)	**INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES AND WEYERHAEUSER'S PHASE II TRACK II REPLY BRIEF**
Staff's Investigation Related to Electric Utility Purchases from Qualifying Facilities.	)	
	)	

REPLY BRIEF OF

INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES AND WEYERHAEUSER

July 12, 2006

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TABLE OF CONTENTS

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TABLE OF AUTHORITIES

Cases **Page**

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I. INTRODUCTION

Pursuant to OAR § 860-014-0090 and Administrative Law Judge ("ALJ") Kirkpatrick's June 23, 2006 Memorandum, the Industrial Customers of Northwest Utilities ("ICNU") and Weyerhaeuser Company ("Weyerhaeuser") submit this Reply Brief addressing the issues in Track II of Phase II of this proceeding. ICNU and Weyerhaeuser believe that their Opening Brief filed on June 7, 2006 anticipated and addressed the vast majority of the arguments and issues raised in the briefs of Staff, PacifiCorp, Portland General Electric Company ("PGE"), and Idaho Power Company ("Idaho Power"). This Reply Brief primarily clarifies ICNU and Weyerhaeuser's position, and responds to arguments that ICNU and Weyerhaeuser did not fully address in their Opening Brief.

II. ARGUMENT

1. The Utilities Have Imposed Obstacles to the Development of Cost Effective Large QFs

Idaho Power and PGE argue that there is no evidence in this proceeding to support the conclusion that the utilities have resisted and thwarted the development of cost effective QFs in Oregon. Idaho Power Brief at 3, n.2; PGE Brief at 5-7. This issue was resolved in Phase I and it is inappropriate for the utilities to make a collateral attack on the Commission's previous conclusions.

The issue of utility resistance to QF development was addressed in the first Phase of this proceeding, when the Commission recognized that QFs larger than 10 MWs face market barriers "that impede negotiation of a viable QF power purchase

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contract with electric utilities." Re Staff's Investigation Relating to Elec. Util. Purchases from QFs, OPUC Docket No. UM 1129, Order No. 05-584 at 17 (May 13, 2005) ("Order No. 05-584"). The evidence that the Commission relied upon in Phase I of this proceeding is still a part of the record, and demonstrates that large cost effective QFs face significant barriers when seeking to enter into contracts with the utilities. See, e.g. Phase I testimonies of Schoenbeck, Breen, Schwartz and Reading (ICNU/100, Schoenbeck/6, 9; ICNU/103, Schoenbeck/3-7, 11-12; Staff/100, Breen/3; Staff/200, Schwartz/19; Sherman/Direct, Reading/2). Idaho Power and PGE also ignore that the Public Utility Regulatory Purposes Act ("PURPA") was passed because Congress found that the reluctance of traditional utilities to purchase power from nontraditional generating facilities impeded their development. Fed. Energy Regulatory Comm'n v. Mississippi, 456 U.S. 742, 750-751 (1982). It was unnecessary for any party to burden the record with additional evidence on this issue because it is an established fact that large QFs face unwarranted barriers when they seek to negotiate contracts with Oregon utilities.

2. PGE Continues to Ignore the Commission's Directives

As explained in ICNU and Weyerhaeuser's Opening Brief, PGE has not complied with the requirements of Order No. 05-584 and refused to identify any specific negotiating parameters or guidelines that should be used to limit its discretion. ICNU/Weyerhaeuser Brief at 7-8. PGE's Opening Brief confirms that PGE is seeking to continue to have unfettered flexibility to refuse to fairly negotiate with large QFs and to limit the development of QFs in its service territory. PGE's refusal to comply with the Commission's desire to adopt specific guidelines for negotiations with large QFs is

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demonstrated by the fact that PGE did not comply with the ALJ's order requiring each party to propose their list of negotiating guidelines. PGE did not provide such a list, as it appears to believe there should not be any guidelines that limit its discretion.

3. Large QFs Should Have the Same Pricing Options as Small QFs

Staff argues that large QFs should not have the same pricing options as small QFs and the utilities should have the discretion to refuse to offer pricing options if they are "inappropriate." Staff Brief at 23-24. According to Staff, this would allow QFs to keep their options open in the negotiation process. Id. While ICNU and Weyerhaeuser appreciate Staff's work in this proceeding, Staff's position on this issue represents a fundamental misunderstanding of the QF-utility negotiating process. The utilities, which have superior bargaining positions, have already stated they do not intend to allow large QFs to select the options available to small QFs; therefore, Staff's position is likely to have the practical effect of denying large QFs the option of avoided cost prices indexed to natural gas prices. This could reduce the accuracy of the avoided costs for large QFs and harm the development of combined heat and power ("CHP") QFs.

Staff appears to have changed its position regarding whether large QFs should have the option to utilize pricing options indexed to gas prices. In the first phase of this proceeding, Staff testified that "the index prices would also form a reasonable basis for negotiation if the QF wanted to negotiate that type of a price structure with the utility." Phase I Hearing Transcript at 179: 20-22 (Breen). Staff has not explained why it now recommends that the utilities should be able to refuse to offer prices indexed to gas to large QFs.

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Staff's current position is also inconsistent with the reasoning behind the Commission's decision to provide pricing options to small QFs. The Commission determined that small QFs should have additional pricing options because "the adoption of more pricing options for QF standard contracts is consistent with our goal, in this proceeding, to more accurately value avoided costs." Order No. 05-584 at 34. The Commission recognized "that a QF is in the best position to select a pricing option that best suits its operations," and "that fairness and administrative ease call for all eligible QFs to have the same set of pricing options . . . ." Id.

This reasoning strongly supports providing large QFs with all the pricing options, including the ability to enter into gas-indexed contracts. The filed avoided cost rates of the utilities include gas price forecasts. The only certain thing about these gas price forecasts is that they will be wrong. These inaccurate gas price forecasts can result in providing inaccurate incentives to QF developers. For example, if the gas price forecasts are too low, then it will be extremely difficult for CHP QFs to enter into QF contracts. Conversely, if the gas price forecasts are too high, then ratepayers may be harmed by higher than necessary payments to CHP QFs. Weyerhaeuser-ICNU/300, Beach/25. The problem of the inherent inaccuracy in the utilities' gas price forecasts should be addressed by providing large QFs with an option to index the gas component of the avoided cost rate to a gas index. The use of gas indexes for large QFs would not shift unwarranted risk to the utilities that base their proxy plants on a gas-fired resource and already are required to mitigate the risk of natural gas fluctuations.

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4. ICNU and Weyerhaeuser Are Not Opposed to Idaho Power's Proposal to Bundle Energy and Capacity Payments

As explained in their Opening Brief, ICNU and Weyerhaeuser have attempted to adopt reasonable proposals that have been offered by Staff and the utilities. ICNU/Weyerhaeuser Brief at 8-12, 14-18. Idaho Power has proposed an "all energy rate" instead of separate capacity and energy payments. Although ICNU and Weyerhaeuser continue to support the proposals made in Mr. Beach's testimony and their Opening Brief as their preferred methods, ICNU and Weyerhaeuser are not opposed to Idaho Power offering an "all energy rate" as long as QFs are rewarded with larger capacity payments if they perform better than the proxy plant.

5. PacifiCorp's Brief Supports ICNU and Weyerhaeuser's Position that Integrated Resource Planning ("IRP") Should Not Be Used to Adjust the Avoided Costs for Large QFs

ICNU and Weyerhaeuser strongly argued against the proposals of Staff and Idaho Power to use the utilities' stochastic IRP models to adjust the avoided costs for large QFs. ICNU/Weyerhaeuser Brief at 13-14. Use of IRP modeling will not provide guidance to QF developers and the utilities, will result in less transparent negotiations, and will provide the utilities with another tool to exacerbate the unequal bargaining positions of the parties. PacifiCorp's Brief supports these conclusions and states that the "IRP-type stochastic modeling proposed by Staff to address dispatchability would be unnecessarily burdensome and time consuming (at a time when QFs desire timely turnaround on indicative price proposals), and should not be required." PacifiCorp Brief at 7-8. ICNU and Weyerhaeuser agree with PacifiCorp on this issue.

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6. Debt Imputation Should Not Be Used to Adjust Avoided Costs

PacifiCorp misinterprets ICNU and Weyerhaeuser's position on debt imputation. PacifiCorp states that ICNU and Weyerhaeuser are "undecided on how the imputed costs should be recognized," and that ICNU and Weyerhaeuser assert that debt imputation should be included in the filed avoided costs rates. PacifiCorp Brief at 20-21. As explained in the Opening Brief, ICNU and Weyerhaeuser are opposed to <u>any</u> use of debt imputation. ICNU-Weyerhaeuser Brief at 24-27. However, if the Commission believes debt imputation should be considered in determining avoided costs, then it should be "reflected in the utility's filed avoided cost calculations, which apply directly to small QFs and are the starting point for negotiations with large QFs." Weyerhaeuser-ICNU/304, Beach/12. Since it is not reflected in the avoided costs for small QFs, there is no reason to impose this phantom cost on only large QFs.

7. PGE Misconstrues the Partial Stipulation Regarding Contract Length

PGE states that all the parties have stipulated that QF contracts for large QFs should be limited to twenty years. PGE Brief at 8. PGE's statement is inconsistent with the partial stipulation on contract terms. The parties to the partial stipulation agreed that QFs over 10 MW should have the right to select a contract length of up to twenty years, but specifically agreed that the "parties have not reached agreement regarding whether the utility and QF should be permitted to enter into PURPA contracts with terms longer than 20 years." PPL/408, Griswold/11.

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III. CONCLUSION

ICNU and Weyerhaeuser urge the Commission to remove a significant barrier to the development of cost-effective QFs in Oregon by adopting reasonable and transparent negotiating parameters and guidelines. The Commission also should ensure greater accuracy in the utilities' avoided costs by providing large QFs with the same pricing options that are available to QFs eligible to receive standard contracts.

Dated this 12th day of July, 2006.

Respectfully submitted,

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July 12, 2006

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Re: In the Matter of PUBLIC UTILITY COMMISSION OF OREGON Staff's Investigation Related to Electric Utility Purchases from Qualifying Facilities.
Docket No. UM 1129

Dear Filing Center:

Enclosed please find an original and six copies of the Reply Brief on behalf of Weyerhaeuser and the Industrial Customers of Northwest Utilities in the above-captioned docket.

Please return one file-stamped copy of the document in the self-addressed, stamped envelope provided. Thank you for your assistance.

Sincerely yours,

<u>/s/ Anna E. Studenny</u>
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Enclosures
cc: Service List

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served the Reply Brief on behalf of Weyerhaeuser and the Industrial Customers of Northwest Utilities upon the parties, shown below, on the official service list by causing the foregoing document to be deposited, postage-prepaid, in the U.S. Mail, or by service via electronic mail to those parties who waived paper service.

DATED at Portland, Oregon, this 12th day of July, 2006.

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