1 **BEFORE THE PUBLIC UTILITY COMMISSION**

2 **OF OREGON**

3 UM 1129

4 PHASE I COMPLIANCE

5 In the Matter of 6 PUBLIC UTILITY COMMISSION OF 7 OREGON 8 Staff's Investigation Relating to Electric Utility Purchases From Qualifying Facilities. 9	STAFF'S POST-HEARING BRIEF

10 **INTRODUCTION**

11 Administrative Law Judge (ALJ) Kirkpatrick described the purpose of this docket as
12 follows:

13 The fundamental purpose of this investigation of the tariffs and standard contracts filed by the electric companies is to ensure that they comply with directives in
14 Order No. 05-584, as well as any other applicable laws, rules or orders…The goal appears to be to fully negotiate and develop tariffs and standard contracts for QFs
15 under 10 MW.

16 Ruling at 5 (Issued November 17, 2005).

17 The same Ruling further adopted a list of 36 issues, many with subparts.

18 The parties subsequently filed testimony on all issues, and a hearing was held. At the
19 conclusion of the hearing, ALJ Kirkpatrick instructed the parties to file post-hearing briefs that
20 specifically identified the issues still in dispute. *See* Transcript of Hearing at 151-152 (ALJ
21 Kirkpatrick).[1] In accordance with these instructions, staff observes that it stands by its
22 recommendations made in its written testimony, and during cross examination, except as
23 expressly stated otherwise in this brief. Staff further notes that a summary of its
24 recommendations is found at Staff/1501. Finally, staff will address each issue in numerical
25 order.

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1 Future references to the transcript will appear as "TR at X."

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THE ISSUES

Issues 1, 2 and 3: Overview issues

As the ALJ noted in her November Ruling, Issues 1, 2 and 3 are very broad and arguably unnecessary. Ruling at 5 (Issued November 17, 2005). Staff agrees with this assessment and as such staff did not submit specific testimony for any of these three issues.

Issue 4: Multiple energy projects

Issue 4 addresses criteria for determining whether a "qualifying facility" (QF) is eligible for standard rates and a standard contract when multiple generating units such as wind turbines are involved. Staff raised Issue 4 to protect the intent of Order No. 05-584, which provides standard rates and contracts only for QFs up to 10 MW. *See* Staff/1000, Schwartz/3. In other words, staff wants to prohibit large projects from being broken up into smaller ones in order to avoid negotiating rates and contracts. *See* Staff Exhibit 1505.

Staff, Idaho Power, PacifiCorp, PGE, ODOE and Sherman County/Simplot signed a Stipulation supporting a settlement on this issue. *See* ODOE Motion and Partial Stipulation (filed February 6, 2006) and ODOE Exhibit No. 8 (Keto). The Fair Rate Coalition (FRC) did not comment on this issue, which it sees as inapplicable to the very small hydro projects it represents. ICNU does not oppose the Stipulation. *See* Staff Exhibit 1505.

Under the proposed settlement, a developer can have part-ownership in more than one project that is in close proximity to another one only under limited conditions. The primary purpose must be to make use of tax credit, green tag or depreciation values. In addition, local governments may own a small share of projects in close proximity to one another, but cannot have an equity ownership interest in or exercise control over the management of the project. *See* Staff Exhibit 1505.

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Issue 5: Security, creditworthiness, damages and termination

Issue 5(a): Security

Issue 5(a)(i): Idaho Power's Section 4.1.6 is reasonable.

Staff stands by its conclusion that Idaho Power's Section 4.1.6 of its standard contract is reasonable. This section allows a QF to demonstrate creditworthiness using a variety of means. If the QF cannot demonstrate creditworthiness, then default security provisions would apply. *See* Staff/1000, Schwartz/6-7.

Issue 5(a)(ii): Security for potential environmental remediation

Staff testified that PacifiCorp should remove its requirement that a QF choosing the step-in rights or senior lien security option under the standard contract must obtain a letter of credit for potential environmental remediation. *See* Staff/1000, Schwartz/13-16.

PacifiCorp does not agree with staff's recommendation. The company states that the risk is unknown and cannot be determined until an evaluation of the specific project site is completed. Further, even if the host company were willing to assume the financial responsibility for environmental remediation, as ODOE recommends be allowed, PacifiCorp would bear the risk that the host company would not have the financial resources to satisfy environmental remediation obligations in lieu of a letter of credit. *See* PPL/302, Wessling/2; ODOE/Exhibit No. 6, Keto/5-6.

Staff stands by its testimony and notes that ODOE shares its concern. Staff/1000, Schwartz/14-16; ODOE/Exhibit No. 6, Keto/6-7. It is unlikely that a small QF could obtain a letter of credit, and the utility's risk of being liable for environmental remediation is minimal.

Issue 5(a)(iii): PGE and Idaho Power definitions for security options

This issue seems to be resolved. PGE agrees to add definitions to the standard agreement using standard legal definitions, provided in response to Staff Data Request No. 56. *See* Staff/1003, Schwartz/22-23. Idaho Power also agrees to provide these definitions and has done so. *See* Staff/1002, Schwartz/4.

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Issue 5(a)(iv): PacifiCorp's definition of "default security"

Staff discusses this issue later in this brief under Issue 35.

Issue 5(a)(v): PacifiCorp's definition of "letter of credit" (Section 1.17)

Staff is satisfied with PacifiCorp's definition. *See* Staff/1000, Schwartz/18-19.

In addition to comments on these sub-issues, staff also recommends the Commission require PacifiCorp to clarify in its standard contract that Section 11.1.4 applies only to QFs choosing the escrow account or letter of credit option for default security. *See generally* Staff/1000, Schwartz/17-23.

Section 11.1.4 of PacifiCorp's standard contract, Material Adverse Change, requires performance assurances as reasonably requested by the company, including the posting of additional default security, in the event of a default under any other agreement to which the QF is a party in cases where the default would have a material adverse effect on the QF project. *See also* Staff/1000, Schwartz/39. Order No. 05-584 states (at 45) that a QF that cannot demonstrate creditworthiness may select at its discretion among four default security options, including step-in rights and a senior lien. The Commission does not require a QF providing default security through step-in rights or a senior lien to post additional default security.

In testifying that Section 11.1.4 is reasonable, staff assumed it applied only to QFs choosing the escrow account or letter of credit option for default security, not the step-in rights or senior lien options. *See* Staff/1500, Schwartz/6-7.

Issues 5(b): Default and Termination

Issue 5(b) generally deals with the standard contracts' default and termination provisions.

Issues 5(b)(i-iv) focus on the utilities' requirements for a QF to identify its minimum energy deliveries. For Idaho Power, staff recommends the company amend its contract to provide for an annual, rather than monthly, energy delivery commitment for QFs relying on intermittent renewable resources, as well as cogeneration facilities relying on industrial hosts. *See* Staff/1000, Schwartz/30-31; TR at 121-124 (Schwartz).

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1 Idaho Power does not agree. *See* Idaho Power/200, Gale/2-6. In general, Idaho Power
2 argues QFs in Idaho have no trouble financing their projects with even more stringent contract
3 requirements. IPCO further claims there is no need to distinguish between intermittent resources
4 and cogeneration for monthly delivery commitment.
5 In response, staff observes:

- The QF cannot control the weather. Wind and water variations are too great to make monthly delivery commitments for the year ahead, and reasonably avoid damages for under-deliveries.
- Small QFs in particular cannot get financing with a high risk of default damages.
- The Idaho PUC set the size eligibility for standard rates far higher than Oregon. So the wind projects developed in Idaho are larger – up to 21 MW so far, instead of 10 MW. Therefore, the Idaho projects may have a different financing strategy. They may have more equity to put into the project, so they can take on more risk, which makes financing easier. Also, to the extent that Idaho has the problem of larger projects being broken up into smaller ones in order to get standard rates and contracts, this may also be a factor that increases the number of QFs in Idaho. That is what staff is trying to avoid with our proposed settlement of Issue 4 in this case. See TR at 117-118 (Schwartz).

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15 The dispute about the "mechanical availability guarantee" (MAG) is also discussed under
16 Issues 5(b)(i-iv). Staff recommends that the Commission allow the utilities to amend their
17 standard contracts to use a MAG based on annual production as the basis for determining default
18 for under-delivery for QFs relying on intermittent resources. *See* Staff/1000, Schwartz/24-26,
19 31-32. PGE does not propose to implement a MAG at this time, awaiting further exploration in
20 Phase II of this proceeding. *See* PGE/300, Drennan-Kuns/8. Idaho Power does not address the
21 MAG in its rebuttal testimony. While PacifiCorp does not address in this phase of the proceeding
22 whether it would like to implement a MAG for standard contracts, staff describes in its testimony
23 the company's favorable views on this subject. *See* Staff/1000, Schwartz/25-26.
24 Issues 5(b)(v, vi, vii and ix) generally concern events of default and the appropriate
25 remedy for a QF defaulting on its contract. Staff has several recommendations in this area.
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1 First, staff recommends that the Commission:

2 Require the utilities to modify their standard contracts to exclude delay of commercial operation as an event of default, including as a cause of termination
3 or related damages, if the utility determines at the time of contract execution that it will be resource-sufficient as of the QF on-line date specified in the contract.

4 *See* Staff/1000, Schwartz/32-33.

5 PGE and PacifiCorp do not agree with this recommendation. Idaho Power did not
6 address this issue in rebuttal testimony. PGE states that projected resource sufficiency or
7 deficiency as of the specified QF on-line date, determined at the time the contract is signed, is
8 irrelevant. If the counted-on resource does not show up, the utility will take actions to replace it,
9 because the utility will have sold power to reach load/resource balance in a projected sufficiency
10 period. *See* PGE/300, Drennan-Kuns/8-9. PacifiCorp states that there is an opportunity cost
11 whether the company is in a resource sufficiency or deficiency period. *See* PPL/400,
12 Griswold/2-3.

13 In response, staff is simply trying to carry out the Commission's order on this point. In
14 Order No. 05-584 (at 47), the Commission stated that security should be provided in the event a
15 QF project is delayed coming on line. However, the Commission provided the following caveat:

16 At the time the contract is signed, we would expect parties to be aware of whether the contracting utility is in a resource deficient or sufficient position. We observe
17 that if a utility is in a resource sufficient position, the contracted-for energy will likely not need to be immediately replaced. Consequently, we do not discern any
18 reason to require additional security requirements in such a situation.

19 This passage refers specifically to whether security should be provided for construction
20 delay when a utility is resource-sufficient, rather than whether a delay should constitute an event
21 of default. However, staff believes that the citation indicates that the Commission found the
22 utility and its customers likely would not be harmed by a delay in QF commercial operation if a
23 utility is resource-sufficient. In addition, if the utility is resource-sufficient, there may be an
24 advantage to the utility and its ratepayers if the QF project is delayed, particularly if market
25 prices are low. *See* Staff/1000, Schwartz/32-33.

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1 Sherman County/Simplot believes that under-delivery also should not be an event of
2 default if the utility is resource-sufficient. *See* Mr. Woodin's direct testimony at 10; rebuttal
3 testimony at 10. Staff and the utilities disagree. Staff found no explicit statement in the order
4 that makes a distinction related to whether the utility is sufficient or deficient for under-delivery
5 default. Further, once the QF is on line, the utility depends on it to meet retail load and make
6 market sales. In addition, the avoided costs the QF already has been receiving are based on a
7 firm proxy resource. QFs that do not wish to make a firm commitment for minimum delivery
8 obligation can sell to the utility as a non-firm resource, priced accordingly. *See* Staff/1000,
9 Schwartz/34.
10 Issue 5(b)(v) concerns various scenarios under which the utility may be able to terminate
11 a QF contract. One aspect of this issue concerns the testing of QF facilities before commencing
12 operation. Staff recommends the Commission require the utilities to modify the testing
13 requirement for achieving commercial operation to take into account availability of motive force.
14 *See* Staff/1000, Schwartz/35. ODOE supports this recommendation. *See* Staff/1004,
15 Schwartz/3.
16 PGE does not agree with staff's recommendation. The company states that it does not
17 limit the number of times the QF may try to demonstrate that it is commercially operable. *See*
18 PGE/300, Drennan-Kuns/9. However, PGE does not address the situation where, due to no fault
19 of the QF's, there is insufficient motive force (wind or water) available at the time the QF is
20 ready to demonstrate commercial operation.
21 It does not make sense to treat such a situation as an event of QF default. Staff's
22 recommendation would ensure that the QF was not penalized for failure to achieve its specified
23 on-line date if the reason was insufficient water or wind for testing to prove that it has achieved
24 commercial operation. *See* Staff/1000, Schwartz/35; TR at 124-125 (Schwartz).
25 Under Issue 5(b)(x), staff recommended that PGE modify its standard contract to provide
26 a payment schedule for QF default damages that takes into account sufficient monies to provide

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for continued QF operations and debt payment when future utility payments are temporarily reduced as a penalty for under-delivery. *See* Staff/1000, Schwartz/42-45.

PGE disagrees with this recommendation for two reasons. First, the company states that the QF has flexibility in setting its minimum delivery obligation, and therefore the company's ability to recover replacement power costs already is limited. Second, PGE states that QF payments should be reduced to off-peak rates when the QF under-delivers the prior year because that recognizes that the company did not receive the full capacity value obligated by the QF. *See* PGE/300, Drennan-Kuns/10.

Regarding the company's first point, PGE confuses the issue somewhat. Replacement power costs are based on the QF's minimum delivery obligation. The QF is not obligated to provide energy or capacity beyond this level, so the utility cannot count on additional levels. Therefore, the utility is not buying replacement power for anything beyond the QF's minimum delivery obligation. Staff's recommended MAG addresses concerns related to setting low minimum delivery obligations in anticipation of worst-case wind and water conditions. *See* Staff/1000, Schwartz/26-32.

PGE's second point misstates staff's testimony. Under staff's recommendation, the total amount of damages recouped is not affected, only the time period over which the damages are collected, and the monthly amounts. *See* Staff/1000, Schwartz/43.

PGE recommends that the Commission not require the company to "automatically adjust its payments to QFs if a QF does not meet its annual minimum delivery," but instead "recognize that PGE has the ability to work with the QF as necessary on a case specific basis." *See* PGE/300, Drennan-Kuns/10.

Staff's recommendation was not intended to mean that the QF must automatically be provided with a payment schedule. Rather, staff's proposal is intended to ensure that the QF can "remain a going concern during the repayment period." *See* Staff/1000, Schwartz/43. In other words, PGE could require the QF to show that it is in danger of "default on its commercial or

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1 financing agreements necessary for its continued operation of the Facility," as PacifiCorp's
2 contract states.
3 If the Commission adopts staff's recommendation, PGE requests guidance with respect to
4 the conditions to be applied to the financing arrangement, including interest rates and maximum
5 amounts to finance.
6 Staff finds both PacifiCorp's and Idaho Power's approaches reasonable. PacifiCorp's
7 contract states: "PacifiCorp and Seller shall work together in good faith to establish the period,
8 and monthly amounts, of such withholding so as to avoid Seller's default on its commercial or
9 financing agreements necessary for its continued operation of the Facility." *See* Staff/1000,
10 Schwartz/43. Idaho Power deducts the accumulated Shortfall Energy Repayment Amount from
11 the next 36 monthly QF payments, in equal amounts. The company applies an interest rate
12 approximately equal to its authorized Oregon rate of return to the outstanding balance. The QF
13 can pay off the balance anytime to avoid further interest payments. *See* Staff/1000, Schwartz/44
14 and 50-51. To the extent PGE wants specific guidance from the Commission regarding interest
15 rates and other provisions, Idaho Power's provisions can serve that purpose. Staff found Idaho
16 Power's use of its authorized rate of return reasonable for the purpose of establishing the interest
17 rate. PGE's authorized rate of return is 9.09%. *See* Order No. 01-777 at 36. Staff also found a 36-
18 month repayment period reasonable.
19 Under Issue 5(b)(xi), PGE agrees to modify its standard contract in Section 10 to reflect
20 reciprocal default terms. *See generally* Staff/1000, Schwartz/41; PGE/300, Drennan-Kuns/9.
21 Also under Issue 5(b)(xi), staff analyzed the utilities' provisions for allowing a QF to
22 "cure" an event of default. *See generally* Staff/1000, Schwartz/38-41. In particular, staff finds
23 the utilities' opportunity to cure periods for achieving first operation date reasonable. Idaho
24 Power provides a 60-day opportunity to cure period, which can be extended by Idaho Power if
25 the QF is making efforts to cure the problem in a "commercially reasonable" time period.
26 PacifiCorp provides a time certain 120 days to cure. For PGE, there is a built-in cure period for

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seller's initial failure to deliver Minimum Net Output, because the company will not terminate the contract until there are two consecutive years of under-delivery. *See* Staff/1000, Schwartz 38-41; TR at 135-138 (Schwartz).

Sherman County/Simplot thinks this is an inconsistent position. *See* rebuttal testimony of Mr. Woodin at 9-10.

Staff stands by its position on this matter. PacifiCorp is reasonably concerned about disputes over how long the cure period should be for a particular event of default if the number of days to cure is not specified. *See* PPL/400, Griswold/3-4. Idaho Power's approach of using what is a "commercially reasonable" time period is a standard business practice, and as such staff finds it also appropriate. Staff accepted PGE's approach as well for reasons explained at Staff/1000, Schwartz/40 and during the cross of Ms. Schwartz. *See* TR at 136-138 (Schwartz).

Under Issues 5(b)(xii, xiii), staff identified a flaw with PacifiCorp's and Idaho Power's respective termination provisions for QF default. Staff recommended the Commission require PacifiCorp and Idaho Power to modify their standard contracts to provide that if a QF is terminated due to its default, the utility may require the QF wishing to again sell to the company to do so subject to the terms of the original agreement until its end date. *See* Staff/1000, Schwartz/36-37.

PacifiCorp agreed with staff and filed proposed revisions to its standard contracts that reflect this recommendation. *See* PPL/400, Griswold/10; §11.3.2 in PPL Exhibits 401 and 402. Idaho Power is willing to modify its contract to include such a provision in its standard contract. *See* Idaho Power/200, Gale/9.

Finally, in its rebuttal testimony, staff discussed a special situation for QFs that are 100 kW and smaller. For these QFs, staff recommends the utilities modify the standard contracts to eliminate under-delivery damages. An alternative for the Commission's consideration is requiring the utilities to modify the standard contracts so that under-delivery damages for QFs

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1 100 kW and smaller may be imposed only for failure to deliver the minimum Net Output for two
2 consecutive years.
3 PacifiCorp responds to FRC's concerns about the default provisions of the standard
4 contracts that it is prudent business practice to include default provisions in QF power purchase
5 agreements in order to provide ratepayers and the company with similar levels of protection as
6 found in other commercial contracts. *See* PPL/302, Wessling/6. However, staff points out that
7 the utilities and ratepayers do not need protection from variations in production from very small
8 QFs – those 100 kW or less. On a similar scale and for similar reasons, the state's net metering
9 law does not require residents or businesses to advise the utility if their net metering facility goes
10 off-line, or allow the utility to impose default damages on the customer for unplanned outages.
11 Further, the Commission will be opening a rulemaking to increase the eligible net metering
12 facility size. *See* Staff/1500, Schwartz/3-4.
13 **Issue 5(c): Damages**
14 Issue 5(c) generally concerns the imposition of damages upon a QF both for an event of
15 default and for termination of the contract resulting from a QF's default. Staff will discuss
16 selected "live" issues that are still in need of resolution.
17 To begin, consistent with Issue 5(b)(iv) discussed earlier, staff recommends the
18 Commission require Idaho Power to revise the damage provision in its standard contracts to
19 accommodate an annual, rather than a monthly, energy delivery commitment. *See* Staff/1000,
20 Schwartz/46-47.
21 Another still-disputed issue relates to the payment of damages if the contract is
22 terminated due to the QF's default. *See generally* Staff/1000, Schwartz/48-49. On this point,
23 staff recommends the Commission direct PGE and Idaho Power to specify that if the standard
24 contract is terminated due to the QF's default, the QF must pay the positive difference, if any,
25 obtained by subtracting the contract price from projected forward market prices for 24 months
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1 beginning with the date of contract termination, for the minimum annual delivery amount

2 specified in the contract. *Id*.

3 PacifiCorp already includes such a provision in its standard contract. *See* Staff/1000,

4 Schwartz/47-48.

5 PGE agrees with staff's recommendations to modify its standard contract to limit the

6 length of time to assess damages in the event of contract termination due to QF default. *See*

7 PGE/300, Drennan-Kuns/3 and 11.

8 Idaho Power does not agree with staff's recommendations. The company does not want

9 any limits placed on its ability to recover termination damages due to the QF's default. *See*

10 Idaho Power/200, Gale/7-9.

11 In response to Idaho Power's objection, staff has the following observations:

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- First, staff's recommendation for termination damages is different than its recommendation for under-delivery damages. Staff's recommendation would not cap the dollar amount of termination damages that the utility may collect *per se*. It would only limit the *time period* over which the utility could claim it has been damaged. Specifically, the time period would be tied to when the company should be able to replace the small QF resource with forward market purchases.

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- Second, staff's proposal would use actual, contemporaneous forward market prices to determine damages. Staff finds appropriate a defined amount for termination damages, equal to the positive difference between market prices beginning at the time of termination and the QF contract price for a period of two years.

19 If replacement power prices are higher than the QF contract prices, these damage

20 provisions make the utility and its ratepayers whole.

21 Staff quotes the following question from Idaho Power's attorney Bart Kline to staff

22 witness Lisa Schwartz to illustrate its point.

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> Q. (from Mr. Kline) Well, let me give you -- I'll give you a hypothetical. Let's suppose that there's four years left on the term of a QF contract, and they terminate the contract early, and without the cap Idaho Power could go to court and try and recover damages for all four years that are left on the contract. And if it was successful, then the benefits of its lawsuit or its recovery of those damages would go to its customers. With the cap in place, it's limited to two. And I guess the question is how does that benefit

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1 customers, to put a cap in place when the utility is gonna have to go to court and prove its damages anyway. How are customers benefiting?

2 TR at 115-116 (Kline).

3 Contrary to what Idaho Power implies in this question, staff's recommendation should
4 avoid disputes and having to go to court altogether for the utility to recover termination damages
5 due to the QF's default. Staff proposes to specify the time period over which damages are to be
6 calculated (24 months), and the manner in which the damages are to be calculated (any positive
7 difference between forward market prices over those 24 months and the QF contract price).
8 Thus staff's recommendation would provide a transparent, easy-calculated damages amount that
9 the QF has agreed to by signing the contract. Further, the loss of the small QF resource would be
10 reflected immediately in the utility's balancing requirements, followed by adjustments to its
11 forward market purchases. Thus, staff determines that the appropriate period of time over which
12 the utility is damaged due to default by small QFs is limited to two years. *See* Staff/1000,
13 Schwartz/48-49; Staff/1500, Schwartz/21-22; TR at 115-116 (Schwartz).

14 A matter that seems resolved related to issue 5c is that PGE agrees with staff's
15 recommendation that it remove from its standard contract the exception for being resource-
16 sufficient for applying damages for under-delivery by a QF. *See* Staff/1000, Schwartz/47 and
17 PGE/300, Drennan-Kuns/11.

18 Staff discusses under Issue 36 another matter that is related to issue 5(c), a cap on default
19 losses the utility may recoup for QF under-delivery or delay in commercial operation date.

20 **Issue 5(d): Creditworthiness**

21 As an overview of this issue, the Commission's Order No. 05-584 did not define all of
22 the creditworthiness tests the utility may use, only two that were at a minimum. *See* Order
23 05-584 at 45. Staff's interpretation of the Order's use of the term "including" is that the
24 Commission did not want to eliminate other means to assess creditworthiness, or delineate any
25 other specific indication of creditworthiness that the utility must review. *See* Staff/1000,
26 Schwartz/6. The utilities agree with staff's interpretation. *See, e.g.*, PPL/302, Wessling/4.

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1 Staff generally concludes that Idaho Power's and PacifiCorp's credit terms and
2 requirements are reasonable. *See* Staff/1000, Schwartz/6-7 (Idaho Power); Staff/1000,
3 Schwartz/9-11 (PacifiCorp).
4 However, staff recommends that PGE modify Section 7 of its standard contract, requiring
5 default security in the event a QF becomes delinquent during the contract term, to provide an
6 exception for becoming delinquent on its construction loan so long as the lender is working with
7 the borrower to become current on loan payments. Staff further recommends that Idaho Power
8 and PacifiCorp make a similar clarification in their respective standard contracts. *See*
9 Staff/1000, Schwartz/7-9.
10 PGE does not agree with staff's recommendation that the company clarify its standard
11 contract in this manner. PGE finds the QF a "risky counterparty" if it is "in default on a financial
12 arrangement essential to the development of a project … regardless of whether the lender is
13 willing to work with them to resolve late loan payments." *See* PGE/300, Drennan-Kuns/6.
14 It may have been unclear to PGE that staff intended the term "construction loan" to apply
15 throughout the term of the power purchase contract – the typical duration of state loans for small-
16 scale projects – not just during the development of the project.
17 PacifiCorp does not agree with staff's recommendation. The company states that it may
18 make exceptions on a case-by-case basis to its requirement that the QF post default security in
19 the event it becomes delinquent during the contract term on its arrangements with the lender, but
20 that it is not appropriate to include language in the standard contract automatically granting such
21 exceptions. *See* PPL/302, Wessling/2.
22 Staff generally recommends standard contract provisions that provide clear direction and
23 apply uniformly to all small QFs. Staff's recommendation would grant an exception to posting
24 default security during the contract term only if the lender is working with the QF to become
25 current on its loan payments. This is an indication that the lender finds the financial difficulty of
26 the QF to be temporary and that the QF project remains viable. *See* Staff/1000, Schwartz/8-9. To

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1 the extent utilities are recommending that they determine on a case-by-case basis whether to
2 grant exceptions to standard contract provisions, there is a greater likelihood for disputes with
3 QFs and need for dispute resolution.

4 ODOE and Sherman County/Simplot do not agree with staff's interpretation of the
5 Order's use of the term "including." Sherman County says that according to staff, the
6 Commission's use of the term "including" gave the utilities carte blanche to demand any indicia
7 of creditworthiness as long as that demand is "reasonable." Sherman County further argues that
8 once a lender or investor has been satisfied as to the creditworthiness of the developer, the utility
9 should also be satisfied, because the lender/investors take more risk. *See* rebuttal testimony of
10 Mr. Woodin at 3-6.

11 However, it is the utility's obligation to make sure that it consummates purchases with
12 creditworthy partners, and if the entity is not creditworthy, that it posts sufficient default security
13 to protect the utility and its customers. *See* TR at 126-127 (Schwartz).

14 ***Issue 6: Tariff list of information requirements and procedures***

15 Staff recommends the Commission direct PGE to provide in its tariff for purchases from
16 QFs up to 10 MW a list of specific project information required to enter into a power purchase
17 agreement. *See* Staff/1000, Schwartz/58-60.

18 PGE does not agree with this recommendation. The company asserts that adding this
19 information to Schedule 201 would be potentially confusing and would duplicate information
20 that is in the standard contract, which is part of the schedule. *See* PGE/300, Drennan-Kuns/13.

21 Staff stands by its recommendation. The standard contract does not provide a summary
22 list of the information the QF is required to provide to obtain draft and executable versions of the
23 filled-in standard agreement. Moreover, staff believes the Commission intended for the utilities
24 to provide this information and, as such, recommends the Commission clarify this matter for
25 PGE.
26 ///

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Staff further recommended that the Commission require that all the utilities' tariffs for QFs up to 10 MW include detailed procedures for obtaining draft and final power purchase agreements, with the following timelines:

a. The Company will provide a draft power purchase agreement to the QF within 15 business days of receipt from the QF of all information required to enter an agreement, as specified in the tariff.

b. The Company will respond within 14 calendar days to any written comments and proposals the QF provides in response to draft agreements.

c. The Company will provide a final draft agreement to the QF within 15 business days of the Company's receipt of any additional or clarifying project information needed.

d. The Company will provide a final executable agreement to the QF within 15 business days of parties' full agreement on the terms and conditions of the draft agreement.

See Staff/1000, Schwartz/61-62.

PGE agrees that the timeline outlined by staff is reasonable for the standard contract and will help address contract administration issues. *See* PGE/300, Drennan-Kuns/13.

PacifiCorp recommends a 15-business day turnaround for each of the four steps, (a. through d.), outlined by staff. However, the company recommends the tariff state that if the QF seeks variations on the contract or has not completed its delivery of information, then the timeline should be extended by the number of days until the necessary information is delivered. *See* PPL/400, Griswold/7-8.

With one exception, this is consistent with staff's recommendations which take into account that the timeline is dependent on whether the QF provides the required information. The exception is that staff recommended a 14-calendar day turnaround for the utility to respond to any written comments and proposals the QF provides after receiving draft agreements (item b.). Staff based its recommended timeline for this step on PacifiCorp Schedule 37. However, as staff observed, the timeline in the tariff appears to relate only to the *final* draft agreement, not the *initial* draft agreement. *See* Staff/1000, Schwartz/61. The result of PacifiCorp's proposal that all steps have a timeline of 15 business days is that the QF would typically be waiting an extra week

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1 for the utility's responses to QF comments and proposals on draft agreements, compared to 14
2 calendar days. Given this small difference in time, and the clarity of having a consistent timeline
3 throughout the process, staff does not object to having a uniform 15-business day timeline for
4 each step.

5 Finally, staff recommends that the Commission direct PGE to specify in its tariff for QF
6 purchases the FERC adjustment factors in 18 C.F.R. § 292.304(e). Staff believes the
7 Commission intended this in its Order No. 05-584 (at 59). *See* Staff/1000; Schwartz/58-59.

8 ***Issue 7: Administrative, technical and licensed engineer requirement***

9 Staff finds reasonable at this time the utilities' requirements that a licensed professional
10 engineer unaffiliated with the QF verify that the facility operates as specified in the contract. For
11 very small packaged systems, staff anticipates exploring such issues in the Commission's
12 forthcoming investigation into interconnection technical standards, procedures and agreements.
13 The Commission may wish to revisit its engineering review requirements for standard QF
14 contracts for such systems at that time. *See* Staff/1000, Schwartz/62-63.

15 Sherman County/Simplot disagrees with staff on this issue. *See* direct testimony of Mr.
16 Woodin at 13-14.

17 ***Issue 8: Impact of QF output changes***

18 Under Issue 8, staff recommends the Commission direct the utilities to amend their
19 standard contracts to treat additional generation resulting from efficiency improvements or
20 necessary equipment replacement as follows:

21 a. The QF will continue to receive the avoided cost rates in place as of the effective date of the current agreement for generating output up to the original
22 nameplate rating specified in the agreement. Payments for generation resulting from any additional capacity installed after the effective date will be based on
23 avoided cost rates as of the date of the improvement or equipment replacement. The contract will be amended at that time to reflect changes in
24 operation or equipment.

25 b. If the total new capacity rating exceeds 10 MW, the QF and the utility will negotiate a new non-standard contract based on avoided cost rates, terms and
26 conditions at the time of the improvement.

See Staff/1000, Schwartz/64-66.

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PGE and PacifiCorp agree with recommendation (b). Both utilities also agree with recommendation (a), but make further recommendations for administrative ease and to reduce disputes. PGE recommends a prorating formula for the portion of the project that would receive updated avoided costs: "For example, if the QF increases the nameplate capacity by 10%, any output from the QF will be split 10% to the new pricing and 90% to the existing pricing." *See* PGE/300, Drennan-Kuns/14. Similarly, PacifiCorp proposes that a new contract price for the QF project be determined based on the weighted average of the existing capacity and energy of the QF as of: 1) the effective date of the original contract and 2) the time of the upgrade or improvement. The new contract price would become effective on the commercial operation date of the upgraded QF project.

Staff views these proposals, which appear to be identical, as clarifications of staff's recommendation that the updated pricing be applied to "generation resulting from any additional capacity installed after the effective date." Staff supports explicit provisions in the standard contract delineating how contract changes would be made if the QF replaces or upgrades equipment.

Issue 9: Insurance

Phase 1 Compliance includes two insurance issues, these issues are:

1. Issue 9.a., which states, "Is it reasonable and appropriate for PacifiCorp and Idaho Power to require the Qualifying Facility to carry insurance only with companies rated not lower than "A-" by the A.M. Best Company? Is it reasonable and appropriate for PGE to require the Qualifying Facility to carry insurance only with companies rated no less than "A" by the A.M. Best Company?"

2. Issue 9.b., which states, "Should the utilities instead require Qualifying Facilities to use insurance companies that are typically and reasonably used for the type of generating equipment used by the Facility?"

For Issue 9.a., Staff points out that a QF should be allowed to obtain insurance from any insurance company that writes insurance coverage in Oregon. The Oregon Department of Consumer and Business Services, Insurance Division (Insurance Division), working with the

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National Association of Insurance Commissioners, is the Oregon agency tasked with ensuring the financial soundness of insurers, promoting the availability and affordability of insurance in Oregon, and ensuring the fair treatment of consumers. The mission of the Insurance Division is, among other things, to license insurance companies and monitor their solvency. *See* Staff 1300, Dougherty/5. In its financial regulation role, the Insurance Division does not use A.M. Best ratings as criteria when authorizing insurers to conduct business in Oregon. *See* Staff 1300, Dougherty/5.

Although the Insurance Division does not use A.M. Best ratings as criteria, staff accurately pointed out in testimony that of the 77 admitted companies in Oregon sampled by staff, 76 were rated "A-" or better by A.M. Best, while one company was not assigned a rating by A.M. Best. The strength of the ratings indicates that financial regulation of insurance companies by the Insurance Division is effective and should be the criteria for determining the insurance company that the QF is allowed to transact business with. *See* Staff/1300, Dougherty/7-8. The Insurance Division has the skill, knowledge, experience, and independence to effectively ensure that insurers in Oregon have the necessary financial stability to conduct business in Oregon.

In rebuttal testimony, the utilities do not present any convincing argument that the Insurance Division is incapable or unable to ensure the financial soundness and solvency of insurers in Oregon. Although PacifiCorp, in its rebuttal testimony, incorrectly refers to the Insurance Division's criteria as a "reduced standard," the company does provide any factual information to substantiate this statement. *See* PPL/600; Reinhart/3.

Requiring a specific A.M. Best rating does not add any value to Oregon customers. In essence, the utilities are mandating an unnecessary requirement for a QF. As staff witness Jack Breen pointed out, "no utility was able to provide an example where it was liable for damages because of the actions of a QF." *See* Staff/100, Breen/10.

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Even though there has not been an occurrence where the utility has been liable for damages because of the actions of a QF, staff points out in testimony that the Oregon Insurance Guaranty Association (OIGA), with a limit up to $300,000 for each liability claim, has been established to protect insureds when an admitted insurance company goes into liquidation and is unable to pay the costs of doing business. *See* Staff/1300, Dougherty/8-9. Although this amount does not reach the level of the required $1 million per claim specified in the standard contracts[2], it is a significant amount. Without a history of claims, Idaho Power can only speculate that $300,000 would not provide adequate back-up protection to cover any claim made against a QF. *See* Idaho Power/200, Gale/10. Additionally, if a claim was to occur, the OIGA has a strong track record for covering claims. According to information provided by the Insurance Division, the OIGA covered 1,103 claims of 12 admitted insurance companies that went into liquidation during the years 2003 through 2005.

Although staff clearly demonstrates that requiring a QF to use an insurer that has a specific A.M. Best rating adds no value to the utilities, customers, or QFs, staff acknowledges that if the Commission decides to use the A.M. Best ratings as a benchmark, then the QF should be allowed to obtain insurance with companies rated not lower than "B+," which is considered "Very Good (Secure)" by A.M. Best. This addresses the concerns of the utilities that QFs should not have insurance obtained from insurers that are considered "Vulnerable" by A.M. Best. Additionally, a requirement for an A.M. Best "B+" rating level would only eliminate a small percentage of insurers authorized to conduct business in Oregon.

For Issue 9.b., staff states that the QF should be able to obtain insurance from any insurance company that is allowed to write insurance coverage in Oregon. It is interesting to note that the National Association of Regulatory Utility Commissioners (NARUC) has concerns about insurance and limiting the providers of insurance when discussing small generator

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[2] The $1 million liability coverage for QFs up to 10 MW is stated in PacifiCorp's PPA Section 13.2.1; Idaho Power's PPA Article XI, 11.2.1.1; and PGE's Schedule 201, Qualifying Facility Power Purchase Information, Section 12.

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1 interconnections. NARUC pointed out in FERC's rulemaking, *Standardization of Small*

2 *Generator Interconnection Agreements and Procedures*, that:

3 > "The very act of requiring insurance would drive up prices because insurance companies would then have a captive market that must have insurance."[3]

4 Additionally, NARUC states in its *Model Interconnection Procedures and Agreement for*

5 *Small Distributed Generation Resources* (emphasis added):

6 > "At no time shall the Interconnection Provider require that the Interconnection Customer negotiate any policy or renewal of any policy covering any liability
7 > *through a particular insurance Interconnection Provider, agent, solicitor, or broker*."[4]

8

9 NARUC observed that by limiting the pool of insurers, there could be a potential to

10 artificially drive up premium costs for a QF. By requiring that a QF only use insurance

11 companies that meet a specific A.M. Best rating or that are typically and reasonably used for the

12 type of generating equipment used by the facility, the utilities are potentially limiting the insurers

13 that a QF could transact business with.

14 Because the QF is paying the bill and pricing is a legitimate concern for a business, the

15 QF should be allowed to choose the insurance company as long as the insurer is allowed by the

16 Insurance Division to write insurance coverage in Oregon. As Staff stated in testimony, the

17 Insurance Division is the appropriate benchmark to use when determining the insurer a QF

18 should be allowed to conduct business with. *See* Staff/1300, Dougherty/6.

19 ***Issue 10: Excluded***

20 ***Issue 11: Force majeure***

21 Staff stands by its testimony on this issue: lack of water and wind should not be included

22 as events of *force majeure* for wind and run-of-river projects. *See* Staff/1000, Schwartz/55.

23 Sherman County/Simplot and ODOE disagree with staff on this issue. *See* rebuttal testimony of

24 Mr. Woodin at 11-12; ODOE/Exhibit No. 6, Keto/6-7.

25

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3 FERC, RM02-12-000, Order No. 2006, issued May 12, 2005; paragraph 303, page 81.

26 4 National Association of Regulatory Utility Commissioners, *Model Interconnection Procedures and Agreement for Small Distributed Generation Resources*, October 2003, page 38.

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1 ***Issue 12: Moved to Phase II***

2 ***Issue 13: Net output***

3 Staff stands by its testimony on this issue. *See* Staff/1000, Schwartz/69. Staff believes
4 the issues raised by Sherman County/Simplot are unfounded. *See* direct testimony of Mr.
5 Woodin at 17. Sherman County/Simplot did not address this matter further in rebuttal testimony.

6 ***Issue 14: Changing standard contract terms***

7 Staff stands by its testimony on this issue and does not believe it is in dispute. *See*
8 Staff/1000, Schwartz/70.

9 ***Issue 15: Natural gas price forecasts***

10 Staff witness Steve Chriss analyzed the natural gas price forecasts submitted by PGE and
11 by PacifiCorp. Mr. Chriss concluded that PacifiCorp's forecast, while lacking in specific
12 supporting data, was reasonable. *See generally* Staff/1100, Chriss/3, 4-9, 17-22.

13 Conversely, Mr. Chriss concluded in his direct testimony that he was unable to determine
14 whether PGE's natural gas price forecast was acceptable because PGE failed to provide
15 sufficient information to support it. *See* Staff/1100, Chriss/3, 4-16. Mr. Chriss then
16 recommended PGE either file additional supporting information for its forecast, or that the
17 company submit a new one. *See* Staff/1100, Chriss/16.

18 Subsequently, PGE filed its rebuttal testimony. *See* PGE/300. While Mr. Chriss did not
19 have an opportunity to file responsive testimony to PGE/300, he did review and analyze it, of
20 course. Upon review of PGE's additional supporting information, staff finds PGE's forecast,
21 while somewhat on the low-side, to be acceptable. Over the life of a long-term contract, a QF is
22 not harmed by selling to PGE over PacifiCorp (and PacifiCorp's natural gas price forecast is
23 reasonable).

24 By reaching this conclusion, staff necessarily rejects ODOE witness Carver's suggestions
25 for the proper method to use to set the natural gas prices for calculating avoided costs. *See*
26 *generally* Staff/1600, Chriss/5-15; TR at 175-176 (Chriss).

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Sherman County/Simplot raised an overarching suggestion that the Commission require the utilities to re-file their compliance filings with updated natural gas prices based on current market conditions. *See* Sherman County/Simplot, Reading/11. Mr. Chriss explained why this idea is not workable.

First, it would require the utilities to essentially continually submit new filings because natural gas prices are always changing. This same notion occurs in rate case filings, where there is always "new" information as the case proceeds. At some point, there is a need to cutoff the submission of new information to allow for the case to proceed to a conclusion. Second, Sherman County/Simplot's suggestion would potentially result in a party trying to "game" the system by submitting a new filing (if the party were a utility) or asking for a new filing (if the party were a QF) whenever the gas price movement favored their respective side of the equation. Finally, the Commission requires new avoided cost filings every two years as it is, and this interval is sufficiently frequent to account for shifts in the marketplace. *See generally* Staff/1600, Chriss/16-17; TR at 170-171 (Chriss).

Issue 16: Appropriate natural gas hubs

Staff witness Chriss concluded that both PGE's and PacifiCorp's method and choice for their respective natural gas hubs is appropriate. *See* Staff/1100, Chriss/23-24. As discussed in Issue 15 above, Mr. Chriss was not persuaded by ODOE witness Carver's suggestion for an alternative method. *See* Staff/1600, Chriss/5-15; TR at 175-176 (Chriss).

Issue 17: Forward price projections

The Commission determined in its Order No. 05-584 that avoided costs during the period of resource sufficiency should be valued at the monthly on-peak and off-peak forward market prices as of the utility's avoided cost filing. *See* Order No. 05-584 at 28. Staff reviewed PGE's and PacifiCorp's compliance filings and found that both companies' forward price projections were reasonable. *See* Staff/1100, Chriss/25-30.

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1 ICNU witness Falkenberg suggested that, in addition to using the monthly forward
2 market prices during the sufficiency period, the Commission should require the utilities to offer a
3 gas market indexed rate. *See* ICNU/200, Falkenberg/9-14. Staff agrees this idea may have merit
4 but has issues to work through, including how it would assess the market value of capacity
5 during the sufficiency period. Staff is willing to work with the parties towards creating a
6 workable market value of capacity if a gas market index rate were applied to the resource
7 sufficiency period. *See* Staff/1600, Chriss/3-4.

8 ***Issue 18: Resource sufficiency/deficiency period***

9 Staff witness Galbraith addressed issues related to setting the resource
10 sufficiency/deficiency period for calculating PGE's and PacifiCorp's avoided costs. Mr.
11 Galbraith's recommendations for each company are summarized at Staff/1200, Galbraith/2.
12 For PacifiCorp, Mr. Galbraith recommended the company include planned "front office
13 transactions" (i.e. short-term purchases) from its 2004 Integrated Resource Plan (IRP) in the
14 load-resource balances used to determine its resource sufficiency period and avoided costs. *Id.*
15 Mr. Galbraith also recommended that the Commission direct PacifiCorp to determine its annual
16 capacity position based on the largest monthly capacity deficit (or smallest capacity surplus)
17 when determining its resource sufficiency period in future avoided cost filings. *Id.*
18 PacifiCorp did not respond to Mr. Galbraith's first recommendation. PacifiCorp has
19 projected 2010 to be its first year of resource deficiency. Including 1,100 MW of capacity and
20 211 average MW of energy from planned "front office transactions" in the company's proposed
21 load-resource balance is not enough to achieve resource sufficiency in 2010.[5] *See* Staff/1202,
22 Galbraith/3. Therefore, staff does not recommend any adjustment to PacifiCorp's filed avoided
23 costs based on its determination of the resource sufficiency/deficiency period. However, staff
24

25 5 The 1,100 MW of targeted capacity from planned "front office transactions" is from PacifiCorp's 2004 Integrated Resource Plan (Docket No. LC 39), Appendix F, Table F.1. Multiplying 1,100 MW of capacity by 1,680 hours in
26 the summer (June – September) on-peak period and dividing by 8,760 hours in 2010 yields 211 annual average megawatts.

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1 continues to recommend including planned "front office transactions" in future calculations of
2 the resource sufficiency/deficiency period when determining PacifiCorp's avoided costs.
3 As to Mr. Galbraith's second recommendation, PacifiCorp witness Widmer stated the
4 company disagreed with it but would not oppose it either. *See* PPL/105, Widmer/7-8. Upon
5 further reflection, staff concludes that this issue involves a minor disagreement over a relatively
6 insignificant matter. Staff agrees with PacifiCorp witness Widmer that, as a practical matter, the
7 difference between staff's and the company's methods "should not have a material impact." *Id*.
8 Accordingly, staff now recommends that the Commission not make any decision on this matter
9 at this time, and instead allow the parties to address this issue on a case-by-case basis in future
10 filings.
11 As to PGE, Mr. Galbraith identified four main problems with the company's filing. *See*
12 Staff/1200, Galbraith/2, 9-13. PGE's testimony filed in response to Mr. Galbraith's concerns
13 was less than staff hoped for. The company did not specifically address any of staff's
14 recommendations but instead broadly dismissed them as "divert[ing] attention from the central
15 purpose of an avoided cost determination." *See* PGE/300, Drennan-Kuns/16.
16 PGE's response unfortunately leaves the record lacking on these important issues. One
17 critical example involves the Port Westward plant. PGE includes Port Westward in its load-
18 resource balance even though the plant is under construction and not yet "used and useful." Staff
19 cannot conclude on this record, even though it may in fact be the proper conclusion, that the
20 plant is a known and measurable resource that is properly included in the company's load-
21 resource balance. Making the single adjustment to exclude Port Westward from PGE's load-
22 resource balance would result in PGE being resource deficient in 2007, not 2009 as the company
23 proposed in its original filing. However, making other staff adjustments to include planned
24 "front office transactions" and to exclude the IRP planning reserve margin would result in a
25 determination that PGE is resource sufficient through 2008. *See* Staff/1701.
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1 While staff thus agrees with PGE's compliance filing that shows the company is resource
2 sufficient through 2008, albeit based on a dramatically different load-resource balance
3 calculation, PGE's failure to respond to the issues raised by staff in direct testimony regarding
4 the determination of its resource sufficiency/deficiency period is problematic. There remains a
5 broader issue that needs to be resolved: How should the Commission treat planned resources in
6 future avoided cost filings? Included under this issue are three related sub-issues: (1) When and
7 under what circumstances should a utility include plants under construction in its avoided cost
8 filing?; (2) Should the utilities include planned short-term purchases in the load-resource
9 balances used to determine their resource sufficiency periods?; and (3) Should the utilities
10 exclude their IRP planning reserve margin from their load requirements?
11 Staff asks the Commission to provide guidance in its order issued in this docket as to the
12 process it wishes to employ to allow staff and the parties to fully explore these important issues.
13 For example, the Commission could direct this issue to be addressed in the Phase II part of this
14 case (recognizing this may require a change to the current schedule) or in the IRP dockets for
15 each utility or in some other docket or forum.
16 ***Issue 19: Utilities' proxy units***
17 Staff witness Chriss reviewed PGE's and PacifiCorp's filings regarding Issues 19(a-c).
18 Mr. Chriss had no issues of concern with the utilities' filings in these areas.
19 Staff witness Gonzalez reviewed PGE's and PacifiCorp's filings regarding Issue 19(d),
20 "Interconnection costs assigned to the proxy unit." Mr. Gonzalez found the interconnection
21 costs assigned to the proxy plants to be reasonable for each utility. *See* Staff/1400,
22 Gonzalez/2-3.
23 Staff is not aware that any other party had concerns under Issue 19(a-d).
24 ***Issue 20: Utilities' modeling***
25 Staff discussed all issues it had with the utilities' modeling under other issues and did not
26 file specific testimony on this issue.

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1 ***Issue 21: AR 495 and green tags***

2 Staff stands by its testimony on this issue and recommends the Commission require PGE
3 and PacifiCorp to amend their standard contracts to provide a waiver of ownership of the non-
4 energy attributes in compliance with Commission Order No. 05-1229. Idaho Power's standard
5 contract already includes such a waiver. *See* Staff/1000, Schwartz/71.

6 ***Issue 22: Meter reading errors***

7 Staff stands by its testimony on this issue. *See* Staff/1400, Gonzalez/4. Staff believes the
8 issues raised by Sherman County/Simplot on this point are unfounded. *See* direct testimony of
9 Mr. Woodin at 17-18.

10 ***Issue 23: Withdrawn***

11 ***Issue 24: PacifiCorp's avoided cost filings in other jurisdictions***

12 Staff did not file testimony on this issue and does not believe any other party did so
13 either.

14 ***Issue 25: Revised Protocol for PacifiCorp***

15 The Revised Protocol is the allocation methodology the Commission adopted to allocate
16 PacifiCorp costs to Oregon. *See* Order No. 05-021. Idaho, Wyoming and Utah have adopted the
17 same Revised Protocol as Oregon, which focuses mainly on generation and transmission costs.
18 The Revised Protocol assigns any costs of new QF contracts that exceed the costs
19 PacifiCorp would have otherwise incurred acquiring "Comparable Resources"[6] on a situs basis to
20 the state that approves the contract. The costs of new QF contracts equal to, or less than, the cost
21 of comparable resources are assigned system-wide. *See* Staff/1000, Schwartz/73.
22 Staff recommends the Commission determine that its process for calculating avoided
23 costs yields power purchase rates for new QF contracts that are not different from costs of
24 comparable resources under PacifiCorp's Revised Protocol. Therefore, Oregon should not be
25

26 6 "Comparable Resource" means resources with similar capacity factors, start-up costs, and other output and operating characteristics. *See* PPL/105, Widmer/10.

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1 exposed to any situs-assigned new QF contract costs as contemplated in the Revised Protocol.
2 *See* Staff/1000, Schwartz/75.

3 ICNU agrees with staff that the Commission should determine in this proceeding that
4 avoided cost rates determined through its approved methodology are equivalent to those of a
5 comparable resource as defined in the Revised Protocol and, therefore, there should be no basis
6 for a situs allocation to Oregon of new QF contract costs. ICNU notes that the Commission's
7 finding should not impact its review of the prudence of any specific resource acquisitions. *See*
8 ICNU/200, Falkenberg/15. This is consistent with the Commission's decision that it will
9 continue its long-standing practice of not approving contracts for individual QF projects, and that
10 the utility retains responsibility for prudent administration of QF contracts. *See* Order No. 05-584
11 at 56.

12 PacifiCorp disagrees with staff and ICNU. The company states, "It would not be
13 reasonable to prejudge or 'deem' the relationship of costs of a New QF Contract to the cost of a
14 Comparable Resource." Instead, PacifiCorp recommends the Commission make determinations
15 on a case-by-case basis in a rate case when the company seeks to include in its revenue
16 requirement the cost of a new QF contract. The company notes that any disputes among states
17 over cost assignment for new QF contracts can be referred to the multi-state Standing
18 Committee. *See* PPL/105, Widmer/11.

19 PacifiCorp mischaracterizes staff's testimony on Issue 25. For example, PacifiCorp states
20 that staff "assert[s] that the *cost* of New QF Contracts in Oregon should be deemed equal to the
21 cost of Comparable Resources as defined in the Revised Protocol" and asks, "What is the basis
22 of Ms. Schwartz's … claims that *prices* determined in this proceeding are equal to those of a
23 Comparable Resource?" *See* PPL/205, Widmer/9-10 (emphasis added).

24 Staff is not asking the Commission to determine that QF avoided *costs* be deemed equal
25 to the cost of comparable resources. Rather, staff recommends the Commission deem the *method*
26 Oregon has adopted for determining the costs the utility avoids through QF purchases, if carried

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1 out correctly by the utility, to yield results consistent with the cost of comparable resources. *See*
2 Staff/1000, Schwartz/75.
3 To calculate standard avoided costs, the Commission requires the utilities to use monthly
4 on- and off-peak forward market prices during the period of resource sufficiency, and the
5 variable and fixed costs of a natural gas-fired combined cycle combustion turbine (CCCT)
6 during the period of resource deficiency. Only QFs up to 10 MW are entitled to standard avoided
7 cost rates and a standard form of contract. For larger QFs, these rates provide a basis for
8 negotiations; FERC adjustment factors also must be taken into account. *See* Staff/1000,
9 Schwartz/74.
10 PacifiCorp routinely makes short-term purchases based on forward market prices. These
11 "front office transactions" reflect the level of market resources that can reasonably be used to
12 delay large, long-term build-or-buy acquisitions. That is why staff recommends that the
13 Commission require PacifiCorp to include the targeted levels of front office transactions from its
14 most recent Integrated Resource Plan (IRP) in the load-resource balances used to determine its
15 resource sufficiency period and avoided costs. *See* Staff/1200, Galbraith/6-9. Given the routine
16 nature of these transactions based on forward market prices, there should be no question
17 regarding the equality of the Commission's methodology for determining standard avoided costs
18 during the utility's resource sufficiency period and the cost of the utility's "Comparable
19 Resources" during such periods.
20 Regarding Oregon's methodology for determining avoided costs during the utility's
21 resource deficiency period, the Commission observed, "Recent utility resource plans identify a
22 natural gas-fired combined cycle combustion turbine (CCCT) as a proxy plant for calculating
23 costs that can be avoided when QF power replaces new utility resources." *See* Order No. 05-584
24 at 22. PacifiCorp stated in Phase I of this proceeding that a natural gas-fired CCCT was its
25 avoidable resource during this period. *See* PPL/100, Widmer/20-23.
26 ///

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In its Phase I compliance testimony, however, PacifiCorp expresses concern over the Commission equating avoided costs based on the costs of its proxy resource for its resource deficiency period with the cost of comparable resources. The Company stated, "Comparable Resources are not pre-defined and all QF's [*sic*] do not have the exact same characteristics of the proxy resource." *See* PPL/105, Widmer/11.

To the extent that the Company's avoidable resource for the deficiency period changes over time, the utility will reflect that in future IRPs and avoided cost filings. Thus, as PacifiCorp's avoided resource changes, the avoided costs will change. However, the *methodology* the Commission uses to determine avoided costs in each case should yield results equivalent to those of comparable resources as they change over time.

Regarding PacifiCorp's concern that QFs do not have the exact characteristics of the avoided utility proxy resource, staff points out that the QF's specific characteristics must explicitly be taken into account for all negotiated contracts. *See* Staff/1000, Schwartz/74. Project-specific costs relative to the proxy plant are not taken into account for standard avoided cost rates available to QFs up to 10 MW. However, that is counter-balanced by also not taking into account small QF benefits such as reduction in line losses, smaller capacity increments, fuel diversity and reduction in emissions costs, even though these benefits bring real benefits to ratepayers relative to the proxy plant. *See* Staff Phase I Reply Brief at 4-5. Regardless, the QF receives payments based on the utility proxy plant — the resource the utility can avoid by buying from the QF. The payments are not based on the QF's costs.

Finally, staff agrees with ICNU's recommendation that the Revised Protocol issue be resolved outside of a rate proceeding in which the revenue requirement impacts related to cost recovery of QF resources may guide some parties' positions. *See* ICNU/200, Falkenberg/16.

Issue 26: Withdrawn

Issue 27: Withdrawn

Issue 28: Withdrawn

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1 ***Issue 29: Withdrawn***

2 ***Issue 30: Liens and encumbrances***

3 Staff recommended that the Commission order PGE to modify Section 3.1.5 of its
4 standard contract to provide an exception for statutory liens. Staff/1000, Schwartz/56-57. In
5 response, PGE agreed to add language to exempt statutory liens. *See* PGE/300, Drennan-
6 Kuns/12.

7 ***Issue 31: PGE Contract § 6.2***

8 Staff stands by its testimony on this issue. This contract provision only asks the QF to
9 take all reasonable measures and exercise its best efforts to perform unscheduled maintenance
10 during off-peak hours. The QF may be able to do so if the generating unit is still performing but
11 unplanned maintenance is indicated. Further, there are no penalties associated with this
12 provision. *See* Staff/1000, Schwartz/57-58. Sherman County/Simplot raised concerns about this
13 provision in direct testimony, but did not respond in rebuttal testimony to staff's perspective on
14 this issue. *See* direct testimony of Mr. Woodin at 18-19.

15 ***Issue 32: PGE Contract § 20.2***

16 Staff recommended that the Commission approve PGE's proposal to modify Section 20.2
17 of its standard contract to read: "By executing this Agreement, Seller releases PGE from any
18 third party claims related to the Facility, known or unknown, that may have arisen prior to the
19 Effective Date." *See* Staff/1000, Schwartz/58. In response, PGE agrees to modify Section 10 in
20 this manner. *See* Staff/1500, Schwartz/10; Staff/1502, Schwartz/12.

21 ***Issue 33: Idaho Power Contract § 3.3***

22 Staff stands by its testimony on this issue, related to Idaho Power's requirement that a
23 hydroelectric QF have the necessary FERC license at the time of contract execution. *See*
24 Staff/1000, Schwartz/71-72. Sherman County/Simplot raised concerns about this provision in
25 direct testimony, but did not respond in rebuttal testimony to staff's perspective on this issue.
26 *See* direct testimony of Mr. Woodin at 19.

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1 ***Issue 34: Idaho Power Contract § 13.2 and 13.4***

2 Staff stands by its testimony on this issue, related to rights of way and access to the
3 seller's facility. *See* Staff/1400, Gonzalez/5. Further, staff believes this issue is now settled. *See*
4 TR at 146 (Woodin).

5 ***Issue 35: Default security amounts in the standard contracts***

6 Staff finds that the amount of default security that PacifiCorp and PGE require to be
7 reasonable. Idaho Power does not specify in its standard contract how it determines the amount
8 of security required. Staff recommends that the Commission direct Idaho Power to modify its
9 standard forms of contract to specify how the company would determine the amount of default
10 security required, in a manner consistent with PGE's or PacifiCorp's standard contract. *See*
11 Staff/1000, Schwartz/19-23.

12 Staff discussed other default security issues under Issue 5(a).

13 ***Issue 36: Cap on Default Damages***

14 Issue 36 is a highly contentious matter concerning a cap on default damages the utility
15 may recoup for QF under-delivery or delay in commercial operation date.

16 Staff recommends that the Commission require the utilities to establish a cap for the
17 standard contracts for default losses that can be recouped pursuant to future QF contract payment
18 reductions, equal to 100% of the QF contract price multiplied by the amount of energy the QF
19 failed to deliver, based on its minimum delivery obligation and contract price for the year in
20 which the event of default occurs. ODOE initially made this proposal, but coupled it with
21 specified capacity factors for each type of QF technology. Staff's proposal does not include
22 capacity factor recommendations. *See generally* Staff/1500, Schwartz/11-22.

23 The utilities do not agree with staff's recommendation. PGE states that while a cap on
24 under-delivery default damages may provide certainty for QF financing, it would not be
25 equitable to the utility and its customers because the QF receives full avoided costs for its
26 expected output so long as it meets its minimum net output under adverse motive force

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1 conditions, even though the expected output is expected to be significantly greater. *See*
2 PGE/300, Drennan-Kuns/11-12. PGE seeks the wrong remedy to this dilemma. Staff's proposed
3 MAG would solve this problem. *See* Staff/1000, Schwartz/24-32.
4 PacifiCorp says there is no basis for assuming that the QF contract value ODOE proposes
5 as a cap on under-delivery default damages would reflect the actual costs the company may
6 incur. The company further states that staff's initial proposal, based on 110% of forward market
7 prices, reflects a more reasonable relationship to actual replacement power costs than ODOE's
8 proposal. *See* PPL/302, Wessling/3. Idaho Power similarly implies that proposals for a cap on
9 default losses are not based on actual, contemporary market prices. *See* Idaho Power/200,
10 Gale/3.
11 PacifiCorp and Idaho Power misconstrue ODOE's proposed cap on default losses, and
12 Idaho Power misconstrues staff's initial proposal as well. Under both proposals, damages are
13 calculated based on the positive difference between actual market prices at the time of default
14 and the QF contract price. However, the amount of these damages that the utility may collect is
15 capped. Under ODOE's proposal, the cap is equal to the total dollar value of the QF contract for
16 the entire year. Under staff's initial proposal, the amount is capped based on 110% of forward
17 market prices. *See* Staff/1000, Schwartz/53-54; Staff/1500, Schwartz/11-21; Staff Exhibits 1503
18 and 1504; TR at 109-110 (Schwartz).
19 ODOE verified staff's interpretation of ODOE's proposal in cross-examination. *See* TR
20 at 100-101 (Keto). First, ODOE Witness Keto agrees that if Staff Exhibit 1504 used ODOE's
21 recommended capacity factors to represent the minimum power delivery requirements — in
22 other words, a 10% capacity factor for wind instead of 33%, and a 20% capacity factor for
23 cogeneration instead of 85% — staff's spreadsheet would accurately illustrate ODOE's proposed
24 cap on default losses. *Id.*
25 Mr. Keto then agreed that the difference between ODOE's recommended cap on default
26 losses, and staff's final recommendation to set the cap on total default loss damages equal to the

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1 QF contract value, is how to establish the minimum power delivery commitment. In other
2 words, staff recommends the QF make an annual delivery commitment for its specific project,
3 with supporting documentation and taking into account the worst motive force conditions, until
4 such time as the Commission adopts a MAG. ODOE instead recommends the Commission
5 establish set capacity factors that would be used to determine the annual delivery commitment.
6 Mr. Keto also stated that it is possible that a wind QF could provide reasonable
7 documentation that under the most adverse motive force conditions, its minimum annual delivery
8 requirement should be set at a level that would be similar to ODOE's proposed 10% capacity
9 factor for wind projects. *Id*.
10 Staff explained in its testimony that for simplification, its example calculations for
11 default caps do not reduce QF delivery requirements for expected adverse motive force
12 conditions, and that this assumption overestimates the utility's unrecovered default losses. It
13 stands to reason that this simplified assumption also overestimates the potential default loss
14 damages the QF would owe the utility. *See* Staff/1500, Schwartz/16.
15 Mr. Keto testified that if the Commission rejects ODOE's recommended capacity factors,
16 ODOE supports staff's initial proposal for a cap on default losses based on 110% of forward
17 market prices, determined at the time of contract execution. Mr. Keto stated in cross-
18 examination that the State Energy Loan Program might be able to finance small QF projects
19 under a default loss cap based on 150% of forward market prices, depending on how the
20 minimum capacity obligation is determined for the standard contract. *See* ODOE/Exhibit No. 9,
21 Keto/2; Transcript (Keto) at 101.
22 Staff concluded after further investigation that a default loss cap based on 110% of
23 forward market prices is too risky for extreme default events. Staff also provided example
24 calculations of the results of a cap based on 150% of forward market prices. The amount of
25 default losses the utility cannot recoup is proportionately less under a cap based on 150% of
26

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forward market prices vs. a 110% cap on such prices. *See* Staff/1500, Schwartz/17-20 and Staff Exhibit 1503.

To summarize this somewhat complex issue, the Commission should adopt staff's recommendation for the following reasons:

- ODOE is a primary lender for small QFs in Oregon. ODOE states that there must be a cap on default losses for under-delivery in order to enable financing of these projects. Similarly, staff has testified throughout this proceeding on the importance for financing of knowing the maximum extent of damages that may be levied for QF default. *See* Staff/1500, Schwartz/13-15; TR at 112 (Schwartz).
- Staff Exhibit 1504 shows that under staff's final recommendation regarding a cap on default losses, only in an extreme default event – when a cogeneration project does not produce power for the *entire year* during a market meltdown when power costs $250 per megawatt-hour — does the QF not pay 100% of the default losses based on market prices at the time of default. In all other cases in these examples, the QF fully pays the default losses. In other words, the zeros in Staff Exhibit 1504 under un-recouped default losses indicate that the utility is receiving 100% of the default losses against actual market prices at the time of default. *See* Staff/1500, Schwartz/19-21; TR at 110-112 (Schwartz).

CONCLUSION

For the reasons stated, staff asks the Commission to follow its recommendation for each issue still in dispute.

DATED this 20th day of March 2006.

Respectfully submitted,

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1 **CERTIFICATE OF SERVICE**

2

3 I certify that on March 20, 2006, I served the foregoing upon all parties of record in this

4 proceeding by delivering a copy by electronic mail and by mailing a copy by postage prepaid

5 first class mail or by hand delivery/shuttle mail to the parties accepting paper service.

6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25 26

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