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BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON
UM 1129
PHASE II -- TRACK 2

In the Matter of
PUBLIC UTILITY COMMISSION OF
OREGON
Staff's Investigation Relating to Electric
Utility Purchases From Qualifying
Facilities.

**IDAHO POWER COMPANY'S
REPLY BRIEF**

July 12, 2006

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I. INTRODUCTION

The Commission in this case is charged with the difficult task of balancing the need to treat QF development in a non-discriminatory manner while at the same time ensuring that utility customers are not harmed. Thus, while the Commission has an obligation to adopt policies that facilitate QF sales to the utilities, it *cannot* do so at the expense of the utilities or their customers.

In their opening briefs each of the utilities have considered QF development as it affects their specific operations and have focused their comments on the issues with the greatest impact on their respective companies and customers. There are, however, two common themes running through the advocacy of all three of the utilities. The first is a concern for the impact that purchases from large QFs will have on the companies' ability to manage their larger resource portfolios. All three utilities have stressed that they must have the freedom to negotiate QF contracts that recognize the impact that large QF purchases will have on their current resource portfolios and their long-term resource plans. The second theme is the utilities' concern that purchases from large QFs not result in higher prices paid for energy by the utilities' customers. As the Commission has recognized on repeated occasions, customers must be held indifferent to QF purchases, and this can be achieved only if utilities pay no more for QF energy than their true avoided costs.

Both Commission Staff and ICNU/Weyerhaeuser appear to agree with the utilities on these points--at least in theory—and many of their recommendations are consistent with the principles advocated by the utilities. However, there are key issues on which the positions urged by either Staff or ICNU/Weyerhaeuser would serve to undercut the very principles they espouse. Idaho Power therefore urges the Commission to carefully analyze the parties' positions on each of the issues, and make findings that will protect the utilities' abilities to operate efficiently and in the public interest, and to ensure that customers are not harmed by its QF policies.

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II. DISCUSSION

A. Idaho Power's Use of Its Integrated Resource Plan ("IRP") Methodology to Determine Avoided Costs for Large QFs in Oregon.

The Idaho Public Utilities Commission ("IPUC") requires Idaho Power to use the IRP methodology to determine avoided costs for large QFs in Idaho. Idaho Power has requested that the Commission allow Idaho Power to use the same IRP methodology to determine the avoided costs that serve as the starting point for negotiations with large QFs in Oregon. The Commission Staff and ICNU/Weyerhaeuser address this request in their Opening Briefs.

The Staff points out that in Order No. 05-584, the Commission allowed Idaho Power to use the methodology approved by the IPUC to calculate *standard* avoided cost rates for small QFs in Oregon. Staff goes on to state that it would not object to the Commission similarly deferring to the IPUC's approved methodology for calculating avoided costs when negotiating with large QFs. Attachment A to Staff's Opening Brief contains Staff's proposed guidelines for the negotiation of QF power purchase contracts for large QFs. Item No. 8 in Attachment A sets out Staff's recommendation that Idaho Power be permitted to use the IRP methodology for calculating avoided costs to be used in negotiations with large QFs in Oregon. Staff's recommendation contains a number of provisos relating to the use of stochastic analyses when the IRP methodology is used.

Idaho Power is willing to include the stochastic analyses described in Item Number 8 in its application of the IRP methodology to contract negotiations with large QFs.

ICNU/Weyerhaeuser's Opening Brief objects to Staff's and Idaho Power's proposal to use the IRP methodology to assess the impact of limited QF dispatchability. ICNU/Weyerhaeuser's objections to use of the IRP model are based on two incorrect assumptions. First, ICNU/Weyerhaeuser bases much of its criticism of the IRP methodology on the assumption that Idaho Power will misuse the IRP methodology to disadvantage large QF developers. ICNU/Weyerhaeuser has presented no evidence in this case that supports its

1 contention that Idaho Power, or any other utility, has or will misuse the IRP methodology in
2 setting avoided costs. ICNU's unsupported allegation is simply waving the bloody shirt.

3 ICNU goes on to say that QF developers generally do not participate in IRP or rate case
4 proceedings due to the expense involved, and it would be extremely difficult for QF developers
5 to understand or verify the adjustments because they are unlikely to have the expertise to test the
6 accuracy of the proposed adjustments. ICNU/Weyerhaeuser's assumption regarding QF
7 developer participation in the IRP process is, at least in the case of Idaho Power, incorrect. The
8 IRP process in Idaho is subject to broad-based participation by a number of parties, including the
9 staffs of the Oregon and Idaho Commissions, environmental groups, industrial customers, and
10 large QF developers, at least one of which is a member of ICNU. All of these participants are
11 actively involved in the development of the IRP. The QF developers routinely utilize the same
12 attorneys and consultants who work with them on QF issues in the IRP process to understand the
13 inputs that go into the development of the IRP. Simply put, industrial customers and QF
14 developers in Idaho are much more active in their participation and review of the IRP process
15 than Weyerhaeuser/ICNU represents.

16 Second, ICNU/Weyerhaeuser objects to the use of the IRP methodology, because it uses
17 Idaho Power's entire IRP resource portfolio rather than the single, hypothetical proxy generating
18 plant to develop avoided cost. ICNU/Weyerhaeuser is correct that the more comprehensive IRP
19 methodology has, in the past, computed avoided costs for some large QFs that are less than the
20 avoided costs derived using the proxy resource. But that does not, as ICNU/Weyerhaeuser
21 assumes, demonstrate that the IRP methodology incorrectly computed Idaho Powers avoided
22 cost for that resource. Under the IRP methodology, the individual characteristics of each large
23 QF project to which the IRP method is applied determines the costs that particular QF project
24 will allow Idaho Power to avoid. It seems to Idaho Power that this result is precisely what the
25 Commission intended when it decided to allow for individual consideration of large QF contracts
26 rather than mechanically applying the standard rates and contracts.

1 **B. Gas Spot Market Prices:**

2 In its Opening Brief Idaho Power explained why it would not be appropriate to require
3 Idaho Power to negotiate contracts with large QFs to purchase energy based on gas spot market
4 prices. Specifically, the Company explained that it had chosen not to rely on base-load gas-fired
5 resources and that it would contravene its IRP to expose the Company to volatile gas prices to
6 any significant degree.

7 Staff agrees that utilities should not be required to offer large QFs the same pricing
8 options made available to smaller QFs under Order No. 05-584, but points out that utilities and
9 QF's should be free to select a gas market option if they both agree. Staff argues that utilities
10 should have the freedom to refuse to offer a particular pricing option where it would be
11 inappropriate to do so—that is, where the resulting price would be inconsistent with the utility's
12 true avoided cost.¹ This position is in harmony with that of the Company.

13 In its Opening Brief, ICNU/ Weyerhaeuser is sympathetic to Idaho Power's position, and
14 suggests that the gas market option be restricted to those utilities that have selected a gas-fired
15 resource as their proxy plant. ICNU/Weyerhaeuser reasons that those utilities are already
16 exposed to the risk of gas prices changes, and further points out that PacifiCorp and PGE have
17 "sophisticated risk management and hedging programs with which they are able to manage gas
18 price risk."²

19 Idaho Power appreciates ICNU/Weyerhaeuser's recognition of the Company' position
20 with respect to gas price risk, but is concerned that its recommendation does not entirely address
21 the Company's concerns. Even a utility that intends to depend on gas-fired resources and that
22 has mitigated its own risk of exposure to gas prices may not be able to protect itself in the face of
23 a large QF contract set at gas spot market prices. As a utility has control of operations of its
24 owned resources, the utility can execute hedging activity that matches the utility's planned
25

26 ¹ Staff's Opening Brief, pp. 23-24.

² ICNU/Weyerhaeuser's Opening Brief, quoting Staff/1900 Chriss/9.

1 operations of the owned resource. In the case of a QF project, a utility does not have control of
2 the operations of the QF resource; thus the utility would be required to execute hedging activity
3 based on the utility's "best guess" as to how the QF project will perform. Moreover, just as
4 utilities can hedge their own gas risk, large QFs can do the same. Allowing them to choose to
5 sell to utilities at gas spot market prices will allow QFs that can hedge their gas risk to enjoy a
6 windfall when gas prices spike—all at the expense of the utility customer.

7 The bottom line is that negotiated prices between large QF's and utilities should reflect
8 the utility's actual avoided cost. As a practical matter, it may be that for a utility that is planning
9 to rely on base-load natural gas-fired resources for the foreseeable future, the gas spot market
10 price will indeed reflect the utility's avoided cost. But there may be circumstances where it will
11 not. For that reason, Idaho Power believes that no utility should be required to purchase energy
12 from large QFs at gas spot market prices unless the utility determines that those prices reflect the
13 utility's true avoided costs.

14 ICNU/Weyerhaeuser opposes Staff's recommendation arguing that it "will have the
15 practical effect of providing the utilities a veto over any choices made by large developers."³
16 This argument misses the mark. The fact is that QF's have the right to sell their energy to
17 utilities at the *utility's* avoided cost, not the price that best suits the QF. If the utility can
18 demonstrate—as Idaho Power has done in this case—that a gas pricing option does not reflect its
19 true avoided cost, *for any reason*, then there is no reason why it should be required to purchase
20 from a QF based on a gas market pricing option. If a large QF believes that the price offered by
21 a utility does not reflect its actual avoided costs, the QF can turn to the Commission. The utility
22 is by no means given any sort of veto.

23 For these reasons Idaho Power is in agreement with Staff that while the parties should be
24 free to agree to select gas spot market prices, the utility should not be required to do so.

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³ ICNU/Weyerhaeuser's Opening Brief, p. 32.

1 **C. Termination and Damages:**

2 Throughout this case, Idaho Power has emphasized the importance of energy reliability.
3 The Company must be able to rely on energy being delivered as promised in order to plan its
4 purchases and sales, and to meet its customer load. Indeed, all parties agree that reliability is
5 critical, and, to varying degrees recommend that QFs be subject to damages for failing to provide
6 promised energy. For instance, Staff agrees that negotiated contracts for QFs that make firm
7 supply commitments should include default and damage conditions that keep the utility and
8 ratepayer whole in the event the QF fails to meet its minimum net output obligation to the
9 utility.⁴ Similarly, ICNU/Weyerhaeuser also appears to agree that damage provisions should be
10 consistent with those contained in standard utility industry contracts.⁵

11 Despite agreement on these general principles, Staff and ICNU/Weyerhaeuser make two
12 recommendations that would serve to undermine their goals. First—while Staff advocates that
13 QFs entering contracts to provide firm energy be subject to damages for under-delivery, Staff
14 advocates that under-delivery be measured on an annual as opposed to a monthly basis.⁶ As
15 pointed out in Idaho Power’s Opening Brief, this recommendation fails to recognize the utility’s
16 need to plan energy purchases to meet monthly, daily and even hourly loads. Moreover, the
17 recommendation that default be measured only on an annual basis is inconsistent with the
18 assertions by both Staff and ICNU/Weyerhaeuser that damage provisions for failure to provide
19 firm energy should be similar to those contained in standard industry contracts. Again, as
20 explained in Idaho Power’s Opening Brief, the Company’s non-QF standard power purchase
21 contracts require sellers to provide specific amounts of energy to be delivered within agreed
22 upon time periods and specify damages for default on these commitments. Thus, an annual
23 commitment is neither adequate for Idaho Power’s planning purposes, nor is it standard industry
24 practice.

25 _____
26 ⁴ Staff’s Opening Brief, p4.

⁵ ICNU/Weyerhaeuser’s Opening Brief, pp. 19-20.

⁶ Staff’s Opening Brief, pp. 8

1 Second – ICNU contends that QF contracts should generally be treated as firm. “Instead
2 of termination, a QF that fails to perform should first have its contract de-rated until it can
3 demonstrate it can provide capacity at a higher level.”⁷ Idaho Power disagrees. Utilities should
4 be free to negotiate default and termination clauses consistent with industry practice. However, if
5 utility customers are to be held indifferent, neither should those provisions be less rigorous.

6
7 **D. Competitive bidding.**

8 As discussed in its Opening Brief, Idaho Power does not advocate that QFs be required to
9 participate in competitive bidding. However it is certainly the case that competitive bidding
10 processes often provide the best information available to the utility as to the costs it can avoid by
11 acquiring QF energy. Therefore, Idaho Power recommends that utilities be allowed to use the
12 results of competitive bidding processes to inform avoided cost calculations for large QF
13 contracts.

14 In its Opening Brief, ICNU/Weyerhaeuser argues against PacifiCorp’s proposal that very
15 large (over 100 MW) QFs be required to participate in competitive bidding.
16 ICNU/Weyerhaeuser also opposes Staff’s recommendation that prices for very large QFs be set
17 based on the results of winning competitive bids, as well as PGE’s proposal that the results from
18 a competitive bid inform negotiations for large QF contracts.⁸ Indeed, ICNU/Weyerhaeuser
19 suggests that when negotiating avoided cost prices that utilities should disregard entirely the
20 results of competitive bidding processes. As an alternative, Weyerhaeuser ICNU recommends
21 that if the Commission intends to allow the utilities to use the results of a competitive bidding
22 process in negotiating avoided cost rates, then the Commission should reject Staff’s proposal and
23 instead allow the utilities to incorporate the information obtained from their bidding processes in
24 their next avoided cost filings. The Commission should reject ICNU/Weyerhaeuser’s position.

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26 ⁷ ICNU/Weyerhaeuser’s Opening Brief, p. 32.

⁸ ICNU/Weyerhaeuser’s Opening Brief, pp. 35-36.

1 It is undeniable that current competitive bidding processes provide the best information
2 about the costs the utility will avoid by purchasing QF energy. Requiring utilities to pretend that
3 they do not have such information would be senseless. Similarly, it makes no sense to require
4 the utilities to delay incorporation of the results of competitive bidding processes for up to a year
5 when it files its next avoided cost study, as such information can quickly become stale.

6 Thus, while Idaho Power takes no position on the particulars of Staff's and PacifiCorp's
7 proposals regarding competitive bidding, it urges the Commission to generally allow the utilities
8 to use the results of competitive bidding processes when negotiating any large QF contract.

9
10 **E. Mechanical Availability Guarantee**

11 Staff recommends that the Commission require the utilities to include a MAG in standard
12 PURPA contracts for firm supply commitments for QFs dependent on intermittent resources.⁹
13 For non-standard PURPA contracts Staff recommends that the utility and QF negotiate whether
14 to incorporate a MAG or a minimum delivery obligation.¹⁰ Idaho Power does not object to
15 including MAGs in any agreements, however; it does not believe that a MAG should be
16 considered in lieu of minimum delivery obligations.

17 Idaho Power understands that QFs dependent on intermittent motive fares such as wind
18 cannot predict with certainty just how much energy that they will produce. However, in
19 voluntarily choosing to invest in intermittent resources, these QFs as independent businesses
20 have presumably made a thorough analysis of the amounts of energy they can reasonably expect
21 to generate. The MAG, when used in conjunction with standard minimum delivery requirements
22 can give the utility some additional comfort that the QF will do all reasonably in its power to
23 meet minimum delivery obligations. However, if the MAG is used *in lieu* of a minimum
24 delivery requirement, then a portion of the risk of investing in an intermittent resource will be
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26 ⁹ Staff's Opening Brief, p. 21.

¹⁰ Staff's Opening Brief, p. 22.

1 shifted to the utility and its customers. This is inconsistent with the letter and intent of PURPA.

2 Staff argues that use of a MAG *in lieu* of minimum delivery obligations would avoid
3 disputes over determination of the QF's minimum delivery obligations and mitigate many of the
4 concerns related to weather, long-term resource forecasting, and default and damage provisions
5 that the parties have raised.¹¹ However, the MAG would do so at the expense of the utility's
6 need for reliability and its right to be compensated when expected amounts of energy are not
7 delivered. For these reasons, utilities should never be required to accept a MAG in lieu of a
8 minimum delivery commitment.

9
10 **III. CONCLUSION**

11 For all of these reasons, the Commission should issues rulings consistent with
12 recommendations of Idaho Power, and allow the utilities the maximum degree of flexibility to

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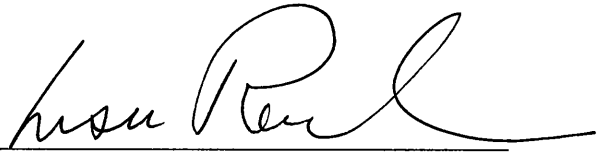
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¹¹ Staff's Opening Brief, p. 22.

1 negotiate terms and conditions for large QF contracts that fully recognize their impact on the
2 utility's resources and costs.

3 Respectfully submitted this 12th day of July, 2006.

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CERTIFICATE OF SERVICE
UM 1129

I hereby certify that a true and correct copy of **IDAHO POWER COMPANY'S REPLY BRIEF** was served via U.S. Mail on the following parties on July 12, 2006:

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Re: UM 1129 Phase II Track 2 – Idaho Power Company’s Reply Brief

Dear Sir or Madam:

Enclosed for filing in the above-referenced docket are the original and five copies of Idaho Power’s Reply Brief. Please contact me with any questions.

Very truly yours,


Wendy L. Martin

Enclosures

cc: UM 1129 Service List