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March 20, 2006

Via Electronic and US Mail

Public Utility Commission
Attn: Filing Center
550 Capitol St. NE #215
P.O. Box 2148
Salem OR 97308-2148

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

Dear Filing Center:

Enclosed please find an original and six copies of the Post Hearing Brief of the Industrial Customers of Northwest Utilities in the above-captioned docket.

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

Sincerely yours,

/s/ Ruth A. Miller
Ruth A. Miller

Enclosures
cc: Service List

CERTIFICATE OF SERVICE

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

DATED at Portland, Oregon, this 20th day of March, 2006.

DAVISON VAN CLEVE, P.C.

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BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UM 1129

In the Matter of the PUBLIC UTILITY COMMISSION OF OREGON Staff's Investigation Related to Electric Utility Purchases from Qualifying Facilities.	)))))))	**THE INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES' POST-HEARING BRIEF**

I. INTRODUCTION

Pursuant to OAR § 860-014-0090 and the Administrative Law Judge's February 7, 2006 Hearing Memorandum and Ruling, the Industrial Customers of Northwest Utilities ("ICNU") submits this Posthearing Brief. ICNU requests that the Public Utility Commission of Oregon ("Commission" or "OPUC") adopt ICNU's proposed methodology for determining whether PacifiCorp is resource deficient or sufficient, adopt ICNU's proposed gas index pricing option for PacifiCorp, and determine that the costs of new Qualifying Facility ("QF") contracts are equal to the costs of comparable resources under PacifiCorp's interstate cost allocation methodology, the Revised Protocol. ICNU also urges the Commission to affirm the specific cost components for PacifiCorp's avoided costs, and require Portland General Electric Company ("PGE") and Idaho Power to file similar information in their future avoided cost filings. Finally, ICNU recommends that the natural gas price forecasts in PGE's and PacifiCorp's filings be updated to ensure their avoided costs are more accurate.

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II. BACKGROUND

On January 20, 2004, the Commission opened an investigation related to electric utility purchases from QFs. On May 13, 2005, the Commission issued its order resolving certain issues, and requiring the three Oregon investor-owned utilities ("IOUs") to file new standard contracts and avoided costs. Re Elec. Util. Purchases from QFs, OPUC Docket No. UM 1129, Order No. 05-584 (May 13, 2005) ("Order No. 05-584").

The IOUs made their compliance filings, and the Commission allowed the filings to go into effect subject to an investigation. Re Elec. Util. Purchases from QFs, OPUC Docket No. UM 1129, Order No. 05-899 (Aug. 9, 2005). This track of this phase of this proceeding is limited to addressing only issues related to the compliance filings. Other QF related issues, including the pricing of non-standard contracts, will be addressed in a separate track of Phase II. Re Elec. Util. Purchases from QFs, OPUC Docket No. UM 1129, Hearing Memorandum and Ruling at 2 n.2 (Feb. 7, 2006); Order No. 05-584 at 3-4, 59. Thus, ICNU's Posthearing Brief does not address issues outside of the narrow scope of the IOUs' compliance filings.

III. ARGUMENT

1. The IOUs Have the Burden of Proof

The IOUs have the burden of proof to establish that their proposed standard contacts and avoided cost rates are just and reasonable. See ORS § 757.210(1) (2003); Pac. Northwest Bell Tel. Co. v. Sabin, 21 Or. App. 200, 213 (1975). The Commission also has the responsibility to ensure that the IOUs' avoided cost rates are just and reasonable. See ORS § 756.040(1) (2003); Pac. Northwest Bell Tel. Co., 21 Or.

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App. at 213. The burden of proof is borne by the utilities "throughout the proceeding and does not shift to any other party." Re PacifiCorp, OPUC Docket No. UE 116, Order No. 01-787 at 6 (Sept. 7, 2001). When other parties dispute the IOUs' proposed contracts and avoided cost rates, the utilities retain the burden to show that their proposals are just and reasonable. Id.

2. PacifiCorp is Resource Deficient (Issue 18)

The Commission should adopt a practical calculation for determining whether PacifiCorp is resource deficient based on the utility's actual need for resources. PacifiCorp's proposed resource sufficiency calculation should be rejected because it produces absurd results. According to PacifiCorp, the Company is resource sufficient, despite the fact that it is unable to cover the summer peak demand for the next five years, and is actively building new capacity, acquiring new resources, and engaging in substantial short-term purchases. ICNU/200, Falkenberg/5-6; Sherman County/ Simplot/107, Reading/10. PacifiCorp is in fact resource deficient, and the avoided cost tariffs the Commission approves in this proceeding should reflect this fact.

The calculation of the resource sufficiency or deficiency period should reflect whether the utility is building or acquiring new resources. As the Commission recently recognized:

> Although a utility may acquire market resources as demand gradually builds at some point, the increase in demand warrants the utility making plans to build or acquire long-term generation resources. At that point, calculation of avoided costs should reflect the potential deferral or avoidance of such generation resources.

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Order No. 05-584 at 27. Read literally, this means that a utility should be considered deficient when it is building capacity.

PacifiCorp's methodology regarding whether it is resource sufficient or deficient does not review whether it is building capacity, but whether the Company is experiencing "a dire capacity shortfall." ICNU/200, Falkenberg/6. The problem with PacifiCorp's proposal is that the utility and Staff really consider it irrelevant whether PacifiCorp can meet the summer peak, so along as it can meet the annual energy requirements. ICNU/200, Falkenberg/5. Ignoring the summer peak is inappropriate because: 1) if PacifiCorp can meet its summer peak, then it will also have enough capacity to meet any peak during the year; and 2) capacity ratings of units are generally lower in the summer. Id. at Falkenberg/5-6. The Commission should reject PacifiCorp's proposal calculation and adopt Mr. Falkenberg's proposal to evaluate whether PacifiCorp is resource sufficient based on whether the utility can meet its summer peak. Id.

By requiring "a dire capacity short fall to exist" for PacifiCorp to be considered "deficient," it will rarely be resource deficient during the initial period of its avoided cost rates. Prudent utility planning often results in building or purchasing additional resources in advance of their immediate need, and will result in postponing any forecasted resource deficit. Thus, under PacifiCorp's calculation, it will nearly always be resource sufficient, even if it is building new capacity and if the purchasing of QF power would result in the deferral or avoidance of resource acquisitions. In contrast, Mr. Falkenberg's proposal is reasonable because it ends the sufficiency period "the moment a

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utility begins the process of actively acquiring a new resource—which for PGE and PacifiCorp is now." Sherman County/Simplot/107, Reading/11.

PacifiCorp's approach also should be rejected because it suffers from other significant flaws, including the use of an unusual and unreliable method to compute reserves and available capacity, the inappropriate reliance upon its GRID computer model, and being inconsistent with the method the utility used to set its 2001 avoided costs. In calculating its reserves, PacifiCorp confuses planning reserves with operating reserves in a manner that provides an unrealistic estimate of available capacity. ICNU/200, Falkenerg/6-7. The GRID model is flawed because it cannot accurately predict the Company's average energy sufficiency because it understates the amount of available energy and can produce absurd results. Id. at Falkenberg/7. Finally, PacifiCorp's proposal should be rejected because its 2001 avoided costs utilized a different calculation. Id. at Falkenberg/8.

3. PacifiCorp Should Offer a Natural Gas-Pricing Option During the Sufficiency Period (Issues 3, 17, 20)

The Commission should adopt ICNU's proposed gas-pricing option for PacifiCorp's sufficiency period. The Commission already has required all three utilities to provide gas-pricing options. Order No. 05-584 at 34-35. However, PacifiCorp has not proposed a gas-pricing option for its sufficiency period, and, if the Commission approves PacifiCorp's calculation for determining its resource sufficiency/deficiency period, then QFs will not have a gas-price option for 2005 to 2009. ICNU/200, Falkenberg/9.

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ICNU's gas price index option would develop the Actual Gas Price Used as the actual gas market index price times an annual heat rate. Id. at Falkenberg/12-13; ICNU/205. The remaining price components were developed from PacifiCorp's fixed prices during the sufficiency period and its gas price forecast. ICNU/200, Falkenberg/13. If the Commission adopts a different gas price forecast for PacifiCorp, then those changes should be incorporated into ICNU's gas price index option. ICNU's proposal would compensate QFs based on energy provided during the High Load Hours ("HLH") with the Non-Indexed Costs, and gas-fired generation during all hours based on the implicit market heat rate. Id.

A gas price index option would be consistent with the Commission's direction to: 1) further develop how to determine the market value of capacity during the sufficiency period; and 2) develop a market price option for PacifiCorp. Order No. 05-584 at 28, 35. A gas market index will assist in the valuation of capacity because the wholesale market price of power is largely determined by the underlying value of capacity and the price of natural gas. ICNU/200, Falkenberg/4, 10-11. Variations in natural gas prices results in increases in wholesale power prices because natural gas is often the marginal fuel during the HLH. Id. at Falkenberg/10-11. In addition, the marginal cost of generation will track gas prices closely when capacity is surplus, and the market price of electricity will increase above the variable cost of marginal gas-fired energy when capacity is short. Id. at Falkenberg/11; ICNU/204.

A gas market index during the sufficiency period will also further the Commission's goal of developing a market indexed rate for PacifiCorp. One rationale for

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having a wholesale market index is that fixed prices can significantly deviate from the underlying gas and power prices. As gas and electricity prices often "move in tandem, use of a gas market index rate" could mitigate the problem of price changes potentially resulting in inequitable and inefficient rates. ICNU/200, Falkenberg/12. In addition, a gas price index would provide gas-fired QFs "a better price signal, as they would have a better sense of their prospects for supplying generation to PacifiCorp, irrespective of the movements in gas prices." Id.

PacifiCorp criticizes ICNU's proposed gas-price index because the utility claims a market price index would be better. PPL/105, Widmer/8-9. PacifiCorp's argument should be rejected because, despite the Commission's request, the utility has not proposed a market price index. Thus, it is inappropriate to reject the gas price index option in favor of a market price index which does not exist. In addition, PacifiCorp's concerns that a market price index would better predict QF costs apply to whether a gas-price index should be used in the deficiency or sufficiency period. Since PacifiCorp has already proposed a gas index price option for the deficiency period, this concern should not impede the adoption of a gas price index for the sufficiency period. Finally, PacifiCorp has failed to raise any specific concerns regarding the details of ICNU's proposed gas price index that would warrant its rejection.

Staff supports the concept of having a gas price indexed rate during the sufficiency period, but raises some concerns regarding the details of ICNU's proposal. Staff/1600, Chriss/3. Specifically, Staff questions whether the difference between on-peak and off-peak prices is fully representative of the market value of capacity during the

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sufficiency period. Id. ICNU does not believe that Staff's concerns warrant rejection of ICNU's proposal, because Staff's alternative to use a fixed price developed at a point in time in the past is far less accurate than ICNU's gas index. Without a gas price index option during the sufficiency period, avoided cost rates will be based on fixed prices that will always be incorrect. In contrast, in ICNU's proposal, the gas index component will always be up to date and the capacity component will be based on market costs at the time the fixed prices are set.

ICNU's primary position is that the Commission should require PacifiCorp to offer a gas market option during the sufficiency period; however, ICNU is willing to consider changes to its proposed methodology that would provide more targeted price signals. ICNU/200, Falkenberg/13. Staff appears to agree with ICNU's primary position that there should be a gas price index, and Staff recommends that, if the Commission does not adopt ICNU's proposal, the parties should further develop a gas price option. Staff/1600, Chriss/4. Despite identifying alleged problems, Staff has yet to offer any solutions. It is inappropriate to delay resolution of this issue, especially when PacifiCorp does not have a market index option for QFs. Therefore, the Commission should require a gas price option for PacifiCorp during the sufficiency period, and either adopt ICNU's proposal or develop its own gas price option. If the Commission does not adopt a gas price option, then ICNU recommends that the Commission require PacifiCorp to file a market price option and provide the parties with guidance regarding how to develop an appropriate gas price index for the sufficiency period.

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4. PacifiCorp's Avoided Costs Should Be Considered Equal to the Costs of "Comparable Resources" Under the Revised Protocol (Issue 25)

PacifiCorp's approved interstate cost allocation methodology, the Revised Protocol, allocates the costs of new QF contracts on a system wide basis, unless the costs of the new QF contract "exceed the costs PacifiCorp would have otherwise incurred acquiring Comparable Resources . . . ." Staff/1000, Schwartz/73. New QFs that exceed the costs of Comparable Resources will be assigned on a situs basis to the state the QF contract was entered into. Id.; ICNU/200, Falkenberg/15-16. Both Staff and ICNU recommend that Oregon's avoided cost rates should be deemed equal to comparable resources because the process that the Commission is utilizing to establish avoided costs for QFs "yields rates for power purchases for new QF contracts that are similar to those for comparable resources." Staff/1000, Schwartz/74-75.

In addition, since each state determines its avoided costs at a different time, there are likely to be differences in each state's avoided costs. Therefore, "the Commission should find that the prices determined in this proceeding are equal to those of a comparable market resource" in order to ensure that different state avoided cost rates are not viewed as Oregon having avoided costs above comparable resources. ICNU/200, Falkenberg/15. This could be a substantial problem as the avoided costs set by each state may differ more widely due to the recent trends in gas and power prices.

PacifiCorp argues against the recommendations of Ms. Schwartz and Mr. Falkenberg because it is possible that the costs of comparable resources and the Company's avoided costs could be different. PPL/105, Widmer/10-11. However, PacifiCorp does not specifically identify any faults or errors with its avoided cost methodology that would result in its avoided costs differing from the costs of comparable resources, as defined under the Revised Protocol. In addition, PacifiCorp's recommended resolution that the issue be addressed in future rate proceedings is fraught with difficulties. ICNU/200, Falkenberg/16. This issue should be addressed "outside of a rate proceeding in which the revenue requirement impacts regarding the cost recovery of the QF resources may guide some parties' positions on this issue." Id. Essentially, PacifiCorp wants to defer this issue until the revenue requirement impacts are known, and it can propose a resolution that will have the largest increase to its Oregon rates.

5. The Utilities' Natural Gas Forecasts Are Inaccurate (Issue 15)

PacifiCorp's and PGE's natural gas forecasts are outdated and should be updated to reflect more current information. PacifiCorp and PGE made their avoided cost filings in early July 2005, including natural gas forecasts based on then current information. There have been significant changes in the natural gas markets since mid-2005, and the forecasts contained with the compliance filings do not reflect current market realities. ODOE/7, Carver/1-7; Sherman County/Simplot/100, Reading/7-10. ICNU believes it would be inappropriate to set new avoided costs based on such outdated and inaccurate information.

Adoption of ICNU's proposed gas price index option would partially remedy the problem of PacifiCorp's avoided costs including inaccurate gas forecasts. Utilizing a gas price index would solve the problem that, regardless of the outcome of this proceeding, the final gas price forecasts will deviate from the future actual gas prices.

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ICNU also recommends that the utilities' natural gas forecasts be updated, despite the fact that Staff raises some legitimate concerns regarding the updating of the natural gas prices forecasts. See Staff/1600, Chriss/5-17. Staff proposes that the Commission examine the merits of the utilities' avoided cost filings at the initial time of filing and in the context of the markets existing at the time of the filing. Id. at Chriss/17. This could be an appropriate method to set avoided costs in the future, because the Commission's review of future avoided cost filings is likely to be more expedited than this proceeding. The review the utilities' avoided cost filings in this docket has been more protracted as the Commission is reviewing both new standard contracts and new compliance filings after a major change in how avoided costs are determined. Thus, since this proceeding has been more drawn out and the utilities and QFs are unlikely to have an order adopting final avoided costs about a year after their compliance filings, it is appropriate to update PacifiCorp's and PGE's inaccurate natural gas forecasts.

ICNU also believes that it would not be inappropriate to update the gas price forecasts in even more expedited avoided cost proceedings. Updating the gas price forecast would be consistent with the trend in Oregon ratemaking of setting the power cost-related portion of rates for PacifiCorp and PGE based on updates at the end of the case. For example, both PGE and PacifiCorp's resource valuation mechanisms are updated at the end of the rate proceedings. In addition, the Commission has recognized that avoided costs should be set and updated to ensure that avoided costs should not be too high or too low. Order No. 05-584 at 29. Regardless of whether the gas price

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forecasts are updated in future avoided cost proceedings, the specific facts of this proceeding warrant an update of the gas price forecasts.

6. The Commission Should Acknowledge the Specific Components of PacifiCorp's Avoided Cost Filing (Issues 3, 19, 20)

The Commission should recognize the specific assumptions used by PacifiCorp in computing its avoided costs because the "information is important for large QFs that will be required to negotiate specific QF contracts with the" utility. ICNU/200, Falkenberg/14. As recognized by the Commission, the utilities' filed "avoided costs are the starting point for negotiations of" non-standard contracts above 10 megawatts. Order No. 05-584 at 12. In the past, the "lack of clarity concerning the actual assumptions and method used by the Company to compute avoided costs" has "created problems in the negotiations for large QFs." ICNU/200, Falkenberg/14. Essentially, it has been difficult for QFs and the utilities to negotiate changes to the filed avoided costs when the QFs did not understand how the utilities' avoided cost number was calculated and what elements were included or excluded in the calculation.

Recognizing the specific components, assumptions and methodologies included in the utilities' avoided costs will assist both QFs and the utilities in negotiating contracts for large QFs. ICNU has introduced information into the record that documents some of PacifiCorp's basic assumptions concerning its avoided costs. Id. at Falkenberg/14-15; ICNU/206; ICNU/207; ICNU/208. PacifiCorp did not dispute this information, and agreed in discovery, with some minor modifications, that ICNU's calculations of the assumptions in its avoided costs are accurate. ICNU/209. ICNU

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accepts PacifiCorp's minor modifications. As there is no dispute on this issue, the Commission should adopt the calculations as being representative of the components and assumptions in PacifiCorp's avoided costs.

The Commission also should require PacifiCorp, PGE, and Idaho Power to include similar information in their future avoided cost filings. The information would reduce the opportunity for disputes between the utilities and QFs, and will result in a more transparent and open negotiating process.

IV. CONCLUSION

The Commission to adopt a realistic methodology for determining if PacifiCorp is resource sufficient, adopt ICNU's proposed gas index option, and require the IOUs to update their gas forecasts. The Commission also should find that the avoided costs approved in this proceeding are equal to the costs of PacifiCorp's comparable resources, and acknowledge the specific components of PacifiCorp's filing.

Dated this 20th day of March, 2006.

Respectfully submitted,

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