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March 20, 2006

Via Electronic Filing and U.S. Mail

Oregon Public Utility Commission
Attention: Filing Center
PO Box 2148
Salem OR 97308-2148

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

Attention Filing Center:

Enclosed for filing in the above-captioned docket is Portland General Electric's Phase II, Track I Compliance Brief. This document is being filed by electronic mail with the Filing Center.

An extra copy of this cover letter is enclosed. Please date stamp the extra copy and return it to me in the envelope provided.

Thank you in advance for your assistance.

Sincerely,

J. Richard George

JRG:am

cc: UM 1129 Service List

Enclosure

BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON

UM 1129

In the Matter of	)	
	)	
PUBLIC UTILITY COMMISSION OF OREGON	)	**PHASE II, TRACK I COMPLIANCE BRIEF OF PORTLAND GENERAL ELECTRIC COMPANY**
	)	
Staff's Investigation Relating to Electric Utility Purchases From Qualifying Facilities	)	

Portland General Electric Company ("PGE" or the "Company") hereby submits its Phase II, Track I Compliance Brief in this proceeding.

I. The Purpose of this Phase of the Proceeding Is Compliance

In this docket investigating electric utility purchases from Qualifying Facilities ("QFs") under the federal Public Utility Regulatory Policies Act of 1978 ("PURPA")[1], the Public Utility Commission of Oregon ("Commission") ordered PGE to make a compliance filing consistent with its Order No. 05-584, including submittal of avoided cost power purchase prices, revised tariffs related to purchases from QFs, and a standard power purchase agreement. PGE made its compliance filing (Advice No. 05-10, Compliance Filing) on July 12, 2005. Here, the Commission must consider whether PGE's filing complied with the policy decisions made in Order 05-584.

It cannot be emphasized enough that this Phase II, Track I of UM 1129, and the subject matter of this brief, concerns compliance, not the rehearing of issues already clearly decided by the Commission in Order 05-584. As Administrative Law Judge Kirkpatrick succinctly stated in her order of March 3, 2006, the purpose of this track is "to address the compliance of standard

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1 Pub. L. No 95-617, 92 Stat. 3117 (codified as amended in various sections of 16 U.S.C.).

QF contracts filed pursuant to Order No. 05-584." In her November 29, 2005 Ruling, ALJ Kirkpatrick ruled that "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 Order No 05-584, as well as any other applicable laws, rules or orders. Issues of compliance have raised clarification questions, however, as well as inquiries about the reasonableness of proposed terms and conditions in context of the directives of Order No. 05-584."

While PGE has made every attempt to comply with the letter and reasonable intent of Order No. 05-584, and supports changes to clarify issues, other parties have made suggestions that the compliance filings should be modified in a manner that clearly contradicts the unambiguous directives of Order No. 05-584.

II. PGE's Natural Gas Forecast Complies with Order No. 05-584 and Is Reasonable

In particular, the Oregon Department of Energy ("ODOE") and Sherman County Court and the J.R. Simplot Company ("Sherman/Simplot") have suggested that the three investor-owned utilities should adopt the same gas forecast methodology, or use the same trading hub. ODOE and Sherman/Simplot essentially propose a standard forecast for all utilities using NYMEX futures as the basis, along with escalation at inflation. (*See* ODOE/Exhibit No 7/ Carver at 4; Rebuttal Testimony of Reading at 11-12.) While PGE does not believe that ODOE's suggested approach is an improvement over the approach used by PGE (*See* PGE/300 Kuns-Drennan/page 21), and Public Utility Commission Staff ("Staff") does not support ODOE's proposal (*See* Staff/1600 Chriss/6 lines 1-2), this proposal would also violate Commission Order 05-584. We do not believe that the Commission was ambiguous in allowing utilities to develop their own individualized gas forecasts using different trading hubs and differing methodologies. The Commission stated: "we decline to require the use of a single natural gas forecast to set avoided cost rates. As Staff notes, utilities have differing views on future natural gas prices and, consequently, there could be legitimate variations among utility forecasts. Moreover, the continued review of avoided costs based on each utility's view of prices is consistent with each utility's actual resource decisions." (Order No. 05-584 at 36.)

Staff, on the other hand, did not suggest that the utilities must utilize the same gas forecast, but contended that PGE's gas forecast was not reasonable because it was too low. (*See* Staff/1100 Chriss/15.) This conclusion was based in large part on an incomplete analysis used by Staff and on mistrust in the quantitative model inputs and assumptions utilized by Cambridge Economic Research Associates ("CERA"), which PGE relied upon for its gas forecasts (*Id.* at 15-16). The suggestion that PGE's forecast is unreasonable or too low is unfounded. PGE's use of CERA for a gas forecast is appropriate for avoided cost calculation. CERA is a well-established, highly regarded research organization. Staff acknowledged that CERA is a firm "well-known for its work in the oil and gas industries. It is safe to assume that they have put a great deal of thought and work into their forecast product" (Staff/1100 Chriss/10 Line 8). Forecasts developed by CERA are available nationally to all facets of the industry, including sellers and buyers. CERA has no incentive to issue an artificially low forecast or one that is incorrect. Thus, PGE has confidence that the econometric forecast conducted by CERA resulted in reasonable avoided costs as filed.

PGE's rebuttal testimony clearly demonstrated that there are flaws in Staff's analysis of PGE's forecast. (*See* PGE/300 Kuns-Drennan/pages 18-20.) Staff relied on only a single spot market price extrapolated for comparison with PGE's 20-year forecast. Staff utilized a non-liquid proxy hub, Kinsgate, rather than the more robust AECO hub, yielding inflated price comparisons. Staff did not use PGE's full 20-year forecast when running their comparison, resulting in only a partial picture. Staff did not compare their forecast with the actual forecast presented by PGE, instead relying on raw CERA data that was only part of the inputs used by PGE to develop its forecast. If Staff had actually compared apples to apples in terms of representative forecasts, it would have discovered that PGE's approach was comparable and definitely reasonable. When PGE's gas forecast is compared to other forecasts such as the Northwest Power and Conservation Council's ("NWPCC"),[2] it is clear that the CERA-based forecast is not unreasonably low, as PGE's actually resulted in higher avoided cost pricing than would NWPCC's. (PGE/300 Kuns-Drennan/21 lines 1-8.)

The natural gas forecast takes effect at the time that the avoided Combined Cycle Combustion Turbine is used to set the avoided cost pricing: 2009 in our current avoided cost calculations. 2009 represents a reasonable point in time where there is a long-term avoidable resource addition consistent with our IRP load/resource balance. Prior to 2009 the Company is in a resource sufficiency period. Staff and Sherman/Simplot raised concerns about utility resource sufficiency periods used in the avoided cost calculations for standard contracts. For PGE the resource sufficiency period for this avoided cost filing extends through 2008, during which period PGE's avoided costs are based on forward market prices. Regardless of the methodology used to determine a resource sufficiency period, the ultimate test is whether the pricing is a reasonable representation of the costs that will be avoided with a new QF supply. PGE's avoided costs meet these criteria and are reasonable.

PGE also notes, as discussed above, that this phase of the docket involves a compliance review of PGE's standard form contract and tariff filing. Obviously, PGE believes that its filing is in complete compliance and is reasonable. Other parties contesting PGE's use of the resource

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[2] Medium Case of the Fifth Northwest Electric Power and Conservation Plan, May 2005.

sufficiency/deficiency periods for setting its avoided cost rates must provide reasons why PGE's filing is noncompliant. These parties have the burden of developing the record with evidence supporting their position as to whether PGE has correctly evaluated resource sufficiency issues and arrived at a reasonable avoided cost. Staff and other parties provided no such evidence, but instead attempt to shift the burden of proof to the utilities. For this reason, PGE's compliance filing should be approved on this issue.

III. Shifting Significant Financial Exposure from QF Lenders to Utilities and Their Customers Is Not Appropriate.

Staff, ODOE and Sherman/Simplot also suggest that the Commission take measures such as capping damages and lowering performance criteria, thereby shifting risks and costs to utilities to make QF projects more financeable. For example, Staff witness Lisa Schwartz admits this objective in answering the following question: "Q: Okay. If because of the cap the utility is unable to recover all of its actual damages, that positive difference is going to be absorbed by the utility and its customers, isn't it? A: That's correct." (Transcript of Cross-Examination Hearing, February 2, 2006 and February 8, 2006 ("Tr.") at 111; see also Staff/1500/Schwartz/13.) She goes on to state: "We are looking at a cap to begin with at all because ODOE is a primary lender in this state. The Small-Scale Energy Loan Program in the state of Oregon is a primary lender for these small QFs, ten megawatts or less and they have stated that they need a cap in order to enable financing." (Tr. at 112.) Sherman County's consultant, Paul Woodin, states succinctly: "Frankly, we want to underscore the fact that unless we have contract terms that a developer can, quite literally, 'take to the bank,' Oregon will not enjoy a robust QF industry." (Rebuttal Testimony of Woodin at 2.) ODOE's testimony is essentially entirely focused on improving the financial picture for QFs and lowering ODOE's lending exposure. (*See, e.g.*, ODOE/Exhibit 6/Keto.)

Without specifically commenting on the goal of making small QFs more financiable, PGE points out, as it has before, that there is no specific evidence in this record that the QF industry has even had project financing issues.[3] Rather, the record contains evidence that suggests that any lack of QF development is related to economic factors in the region: specifically, historically low avoided costs due to the availability of low-cost power (in particular hydropower) on the wholesale market. (*See* Staff/200 Schwartz/5.) Moreover, although QF contract numbers in Oregon are moderate, the penetration of QFs in Oregon is likely appropriate, given Oregon's ranking in terms of power rates. (*See* PGE Exhibit/100 Drennan-Kuns/24-25.)

We also point out that shifting the balance between utility customer impact and financeability of QF projects so heavily in the direction of QFs is not appropriate in light of Order No. 05-584. In that order, this Commission stated: "In balancing the goals of facilitating QF contracts while sufficiently protecting ratepayers, we recognize that the primary aim is to ensure that ratepayers remain indifferent to the source of power that serves them." ODOE, Sherman/Simplot and, in some cases, Staff, would have the primary aim be to make QFs more financeable regardless of utility customer impact.

This imbalance has the primary effect of protecting ODOE. It suggests that the State Energy Loan Program ("SELP") is unable to accept the associated risk of QF development, but feels it is appropriate for utilities and their customers to accept those risks. This may not be good public policy. PGE's customers are a subset of the entire state population, which otherwise bears

[3] Indeed, prior to this docket QF contracts did not contain damage caps, limitations on insurance requirements or lowered performance standards, yet there was no evidence presented that QFs could not obtain financing under such conditions.

the financial risk for QF borrowing from ODOE under SELP.[4] Shifting the risk to a smaller number of individuals through "must take" contracts where such individuals have no voice as to whether they wish to incur such risk may not be appropriate.[5]

IV. Specific Contract Provisions

For the most part, other than generally seeking modifications to make projects less risky to financing entities, parties did not have significant objections to PGE's standard form contract. Staff and others raised in testimony certain issues with PGE's standard contract, and PGE has already agreed to make most of these changes, including: 1) requiring PGE to also make representations and warranties; 2) making default terms also apply to PGE; 3) removing the exception for applying damages for under delivery from the standard contract for being resource-sufficient; 4) limiting collection of default damages to two years after the event of default; 5) excepting statutory liens from the QF representation and warranty against liens on the facility; 6) making the release of claims specifically apply to third-party claims and not those of the QF; and 7) adding definitions for cash escrow, letter of credit, step-in rights, and senior lien.

A few specific contract provisions, though, remain contested and bear discussion. In particular, Sherman/Simplot finds offense with PGE's lack of a specific opportunity to cure. (*See* Woodin, Phase I, Compliance Direct Testimony at 11.) PGE's contract, however, takes a

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[4] *See* Oregon Constitution, Article XI-J, which establishes the SELP loan fund and provides for it to be funded by bonds paid through taxes levied annually upon all the taxable property in the State of Oregon or through other revenues by the Legislative Assembly.

[5] Several parties cite intangible benefits of QF development to utility customers, but provide no specific evidence in this docket about such benefits. (*See, e.g.*, Wooden, Rebuttal Test. at 3; Tr. 96 (Keto).) Again, these are "must take" contracts, where customers will have no choice whether they want to subsidize or absorb their financial risk. PGE's customers already pay a public purpose charge pursuant to ORS 757.612 to fund QF-type renewable resources, and the Legislature has suggested pursuant to ORS 757.612(4) that utilities collecting that charge be exempt from other similar efforts (*e.g.*, State PURPA, ORS 758.505-555). In addition, PGE's customers always have the option to choose to pay for renewable power through options such as PGE's "Green Source" and "Clean Wind" programs.

different and reasonable approach to the issues a cure period attempts to resolve. Specifically, with respect to a QF's performance under PGE's contract, an event of default does not arise until the seller has failed to deliver its Minimum Net Output for two consecutive years. (*See* Advice No 05-16, Appendix 1, Schedule 201, Section 10.1.4.) PGE also allows the QF to choose its own reasonably verifiable minimum net output number (*Id*. at Exhibit A). By allowing the QF to develop its own minimum target and giving it a long period to overcome problems and increase output to meet the goal, PGE attempts to create up-front flexibility and certainty with respect to the QF's performance commitment, rather than have the potential for many default situations and the uncertainty of whether a QF will be able to cure such defaults. In any event, under PGE's contract, even if any type of default were to occur and the agreement was terminated, the QF still is entitled to require PGE to purchase its output under PURPA and enter into a standard contract. In that case, the agreement could be renewed on the same terms, or PGE could require a new agreement based on then current and applicable avoided costs. (*See Id*. at 10.4.)[6]

Another contested contract clause is the event of default due to a failure to meet the on-line date for the facility. (*See, e.g.*, Woodin, Phase I, Compliance Direct Testimony at 10; Staff/1000 Schwartz/33; Tr. 136 (Schwartz).) The arguments against that clause appear to suggest that such a default should not exist during a period of resource sufficiency because the utility does not need the output of the QF. However, whether or not the utility is resource-sufficient, it still will incur damages. Even when PGE is resource-sufficient, it is still purchasing power and also incurring costs to accurately plan how it will meet its load. If a QF does not

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6 Staff found that PGE's contract was reasonable in this respect because it contains a "built-in cure period for Section 10.1.4, 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. Thus, the QF can cure the initial year of performance failure." (Staff/1000 Schwartz/40.)

come on-line when anticipated, PGE likely will be harmed regardless of whether it is resource-sufficient or not. In order to obtain certainty from a planning standpoint, and to avoid incurring unnecessary costs related to power purchases, PGE makes time "of the essence" with respect to a specific contract and the avoided cost pertinent to that contract. Moreover, PGE does not choose the facility's on-line schedule, and QFs should be encouraged to provide dates that are reasonable and achievable. As discussed above, if the QF does not meet its on-line date, and the contract is terminated, it still can require PGE to enter into a new contract at some time when it is actually ready to come on line.

Finally, some parties contest the omission of weather events resulting in lack of wind or water as *force majeure* events under PGE's standard contract. (Woodin, Phase I, Compliance Direct Testimony at 9, 15; ODOE/Ex. 6/Keto/6-7.) PGE does not include such weather events, as in most instances such events are reasonably anticipated and modeled. (*See* Staff/1000 Schwartz/55; Idaho Response to Staff Data Request 20.) PGE does attempt to reasonably accommodate weather events by allowing a QF to set its own minimum output, taking into consideration weather, maintenance outages, etc. As discussed above, PGE has a very flexible default term with respect to delivery of the required minimum output on a yearly basis (consecutive two years failure before default). For the same reason we discussed with respect to a right to cure provision—that PGE has attempted to resolve the same issues, but in a different way—it is not appropriate to make weather related events *force majeure* events.[7]

[7] Staff supports the utilities positions that lack of water or wind is not an event of *force majeure*. (*See* Staff/1000 Schwartz/55.)

V. Conclusion

The purpose of Docket UM 1129 is to implement those portions of federal PURPA in which the federal government has specifically delegated authority to this Commission. Specifically, the federal government gave jurisdiction to this Commission to set a threshold for a standard contract and standard rates. 18 CFR 292.305(c)(2). The federal statute and rules do not specifically talk about standard contract terms. However, we understand and support the creation of a standard contract to facilitate small QF development, and believe that our standard contract as filed does so. Federal PURPA is specific, though, that the rates for purchases by utilities: "[s]hall be just and reasonable to the electric consumers of the electric utility and in the public interest," and that the rate cannot "exceed the incremental cost to the electric utility of alternative electric energy [*i.e.* avoided cost]." (16 U.S.C. 824a-3; *see* 18 CFR 292.304(a)(2).) We believe that modification of standard contract provisions specifically for the purpose of shifting financial risks from lenders to utility customers is not allowed under such constructs. PGE acknowledges that there may be cases where significant performance and financial problems of QFs need to be addressed in order to assure viability of those QFs and to minimize harm to the utility and its customers. When such significant performance and financial problems occur, they generally should be addressed on a case by case basis by the utility and the QF. Otherwise, mandating provisions such as caps unrelated to actual damages and lowered performance standards will magnify the impact of significant performance and financial problems on utility customers. This would shift the balance too far away from the objective set forth by this Commission of making the utility customers indifferent to where their power is coming from.

DATED this 20th day of March, 2006.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that I have this day caused the PHASE II, TRACK I COMPLIANCE BRIEF OF PORTLAND GENERAL ELECTRIC COMPANY to be served by electronic mail, and for those parties who have not waived paper service, by First Class US Mail, postage prepaid and properly addressed, upon each party on the attached service list, pursuant to Oregon Administrative Rule 860-013-0070.

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

/s/ J. RICHARD GEORGE____________________
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