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BEFORE THE PUBLIC UTILITY COMMISSION OF OREGON

IN THE MATTER OF THE PUBLIC UTILITY COMMISSION OF OREGON STAFF'S INVESTIGATION RELATING TO ELECTRIC UTILITY PURCHASES FROM QUALIFYING COUNTY FACILITIES	)	DOCKET NO. UM 1129 POST HEARING BRIEF BY SHERMAN COUNTY COURT AND THE J. R. SIMPLOT COMPANY

This Post Hearing Brief is filed on behalf of the Sherman County Court and the J. R. Simplot Company ("Sherman/Simplot") pursuant to direction from the Administrative Law Judge in the above captioned matter. Although this brief addresses many of the significant issues raised in this case, it does not address ALL of the issue. The lack of attention to an issue raised in our testimony should not be read as acquiescence on that issue.

THIS COMMISSION IS REQUIRED BY FEDERAL LAW TO ACTIVELY ENCOURAGE THE DEVELOPMENT OF COGENERATION AND RENEWABLE RESOURCES

The Commission[1] is at a critical juncture in this docket. In its review of the Utilities' compliance filings it is important to keep in mind that this Commission is charged by Federal law to actively encourage the development of cogeneration and small power production facilities through a pro-active implementation of PURPA. [2] This mandate has been repeatedly affirmed by the Courts:

> The basic purpose of § 210 of PURPA was to increase the utilization of cogeneration and small power production facilities and to reduce reliance on fossil fuels. See *FERC* v. *Mississippi*, 456 U.S., at 750.

Am. Paper Inst., Inc. v. Am. Elec. Power Serv. Corp.,461 U.S. 402, 417 (1983). In Southern California Edision v. FERC[3], the D.C. Circuit court observed that the purpose of PURPA was:

> [T]o encourage the development of facilities that generate electricity using renewable resources and facilities engaged in cogeneration of electricity and useful heat or steam that might otherwise be wasted . .. . and to overcome the reluctance of traditional utilities to buy from, and sell to, those alternative producers…

Id. at p. 19.

The D.C. Court's finding that utilities are 'reluctant' to do business with QFs should instruct this Commission's deliberations in this phase of UM-1129. It is certainly no accident that Oregon (unlike Idaho) has had almost no QF activity over the last twenty years. There can be no doubt that without the constant vigilance, active encouragement, and forceful implementation of PURPA by this

[1] The Public Utility Commission of Oregon.
[2] Pub. L. No. 95-617, 92 Stat. 3117, Public Utilities Regulatory Policy Act of 1978

Commission, that Oregon will be doomed to face another two decades without the benefit of a robust and active QF industry.

ALL THE PIECES OF THE PUZZLE MUST FALL INTO PLACE IN ORDER FOR THE COMMISSION TO FULFILL ITS PURPA OBLIGATIONS

As Mr. Woodin pointed out in his direct testimony:

> It is simply not possible to have a successful PURPA program unless all the various pieces of the puzzle fit. We must not only have attractive rates, but we must have contract terms that enable financing and are attractive to investors. The term of the agreement must be long enough to amortize the costs of development.[4]

Mr. Woodin's testimony on these matters should be afforded greater weight than others because he is actually a developer of QF and renewable energy projects. Mr. Woodin testified that the compliance filings made by the three IOUs in this docket will not result in a healthy QF industry in Oregon.[5] The reasons for his conclusion are detailed below. The Commission is urged to remain cognizant of Mr. Woodin's warning that "unless all of the various pieces fit" the Commission's mandate to encourage the development of a healthy QF industry will not be fulfilled.

The compliance filings made by the three investor-owned utilities suggest that they either do not understand this Commission's obligations under PURPA or

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[3] 195 F.3d 17 (D.C. Cir. 1999)
[4] Sherman Simplot 105, at pp. 2-3.

they hope to subvert the ability of the Commission to fulfill those obligations. The fact that no new QF contracts have been executed since the compliance filings were made is compelling evidence that the compliance filings are *per se* defective. Sherman/Simplot respectfully submits that adoption of its resolution of the remaining disputed issues will result in a healthy QF industry for Oregon.

THE COMPLIANCE FILING AVOIDED COST RATES ARE TOO LOW

The avoided cost rates contained in the utilities' compliance filings are too low for two reasons. First, the artificially low avoided cost rates are due, in part, to a misreading of the Commission's Order dealing with "surplus periods" in determining the date of first need for capacity. The second reason the rates are too low is that the utilities use a natural gas price forecast that is stale and unrealistic in light of current known and measurable market conditions.

SUFFICIENCY PERIOD
OR
'LET THE GAMES BEGIN'

The Commission's order in this Docket has been misconstrued by the utilities and the Commisson's Staff in order to artificially lengthen the "surplus period" such that the avoided cost rates are set too low. The Commission's

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[5] *Id.*

decision on the surplus period issue is based on the deferral or avoidance of a planned resource. Specifically the Commission ruled:

> The calculation of avoided costs when a utility is in a resource deficient position should reflect longer term resource decisions that are subject to deferral or avoidance due to QF power purchases. Although a utility may acquire market resources as demand gradually builds, <u>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</u> resources.

[Order 05-584, UM1129, p. 27. Emphasis provided.]

It is clear that the Commission is focusing on <u>when</u> a utility <u>makes "plans</u> to build or acquire" long-term resources, rather than on the type of resource being acquired. As Dr. Reading testified in his direct testimony,[6] both PGE and PacifiCorp are currently acquiring resources. Furthermore, Staff's approach[7] misses the mark by looking at the utilities' estimates of significant shortfall of both capacity and energy and not at the fact that the utilities are currently acquiring and planning to acquire resources that can be deferred.

In his direct testimony Dr. Reading offered evidence demonstrating that a sufficiency period should not be used in calculating avoided cost rates.[8] Dr. Reading was troubled by the fact that both PGE and PacifiCorp are CURRENTLY ACTIVELY ACQUIRING RESOURCES while at the same time claiming to be

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[6] Sherman Simplot 100, at pp 3-4.
[7] Staff/Galbraith 1200, at p. 4.

resource surplus solely for purposes of acquiring QF resources. He called that troubling situation a "paradox".[9] It is however, more than a paradox, it is hypocrisy; and although such hypocrisy is not unexpected, it should not be tolerated. It was precisely that type of gamesmanship that caused the Idaho Commission to declare that no utility can claim a surplus period for purposes of setting avoided cost rates in Idaho.[10] If this Commission still wants to use a sufficiency period in light of such behavior, that surplus period should end the moment a utility begins the process of actively acquiring a new resource – which for PGE, PacifiCorp and Idaho Power is now.

NATURAL GAS FORECAST
OR
'DON'T BOTHER ME WITH THE FACTS'

The question before the Commission (in this compliance phase of the docket) regarding natural gas price forecasts is a simple one: "How old is too old?" This docket was initiated well over two years ago with no end in sight on the near term horizon. The utilities' compliance filings, that were made in July of 2005, contain avoided cost rates based on natural gas price forecasts that were made sometime prior to July 2005. This phase of UM-1129 has already consumed more time than a general rate case. At some point the information contained in the

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[8] Sherman Simplot 100, at pp. 3-6.
[9] *Id.* at p. 6.
[10] *See* Sherman Simplot/Reading 100, at p. 6.

original filing should be made current for known and measurable changes. Dr. Reading testified that now is the time to update the natural gas forecasts. According to Dr. Reading, the natural gas prices used by the utilities do not reflect reality, or in his words; "current market realities."[11]

Not surprisingly, the utilities have been resistant to updating their natural gas forecasts because doing so will result in higher avoided cost rates – and quite possibly allow the QF industry to actually develop in Oregon. Remarkably, however, the Staff also insists on using stale data in setting Oregon's avoided cost rates. In fact, the data is not only stale, it is demonstrably inaccurate. The Staff natural gas witness, Mr. Chriss, provided the following testimony on this point:

> Q. And do you believe your statement is true, that the Commission should examine the merits of a utility's avoided cost filing at the time of the initial filing? Is that true regardless of how dramatic intervening events might be since the time of the initial filing?
>
> A. Yes.

Tr. 170.

The Staff's remarkable refusal to re-examine natural gas price forecasts notwithstanding, this Commission has ruled that it does not intend to wear blinders when it comes to updating inputs for purposes of setting avoided cost rates:

> Understanding that circumstances may change to make existing avoided cost rates either too low or too high, we recognize that

[11] Sherman Simplot 107, at p. 9.

> other parties besides the utility may wish to address avoided cost rates on an unscheduled basis. Consequently, we will exercise our discretion, when appropriate, to direct a utility to make an avoided cost filing between scheduled filings. The Commission may institute a supplementary proceeding to review a utility's avoided costs on its own motion or at the request of any party. <u>We encourage parties to notify the Commission when it may be appropriate to review avoided cost rates between filings deadlines.</u>

Order NO. 05-584, p. 29. Emphasis provided.

The Commission should consider the testimonies of Dr. Reading for Sherman/Simplot, ICNU witness (Mr. Falkenberg, ICNU 200) and ODOE witness (Mr. Carver, ODOE 7) as notice that it is now appropriate to update the utilities' avoided cost rates in light of changed natural gas prices and changed natural gas price forecasts.

CONFUSION SURROUNDS THE COMMISSIONS CREDITWORTHINESS PROVISIONS FOR STANDARD CONTRACTS

The road to a robust QF industry is, indeed, a long one. As noted by Mr. Woodin, however, every piece to the puzzle is as important as the next piece. In other words, it is just as important to have finance-able contract terms and conditions as it is to have adequate rates. Some considerable confusion has arisen over the following passage from the Commission's order:

> We are persuaded that all QFs should be required to establish creditworthiness by making a set of representations and warranties that the QF has good credit, **including** that it is current on existing debt obligations and has not been a debtor in a bankruptcy proceeding within the preceding two years. Requiring a party to a contract to enter the contract with good credit is a reasonable and prudent requirement.

Order No. 05-584, p. 45. Emphasis provided.

Apparently, according to the Staff, the word "including" gives the utilities carte blanche to demand any indicia of creditworthiness as long as that demand is "reasonable." Unfortunately, according to Mr. Woodin, "reasonable" is in the eye of the beholder.[12] As noted by Idaho Power, and observed by Ms. Schwartz, most QF developers form new single purpose legal entities to facilitate project financing.[13] It is not possible to require more than the representations identified in the above quoted passage from such an entity. Giving the utilities flexibility in devising their own creditworthy standards outside of the scope of this proceeding, defeats the underlying purpose of having this proceeding. QF developers need to know, up front, what will be required of them and the utilities need guidance from the Commission as to what they are allowed to require of QF developers.

[12] Sherman/Simplot 105, at p. 3
[13] Staff 1000, at p. 7; Staff 1002, Schwartz/3.

Mr. Woodin testified that if a lender or investor has been satisfied as to the creditworthiness of the developer then the utility should, by definition, also be satisfied. This is because the lender and/or investor assumes almost all of the risk of a QF's default. This is especially true when the utility claims to be in a surplus period. For the utility to place more stringent creditworthiness criteria than the lender and or investor require is inappropriate. They don't carry the risk that the lender or investor do.

Unfortunately, use of the word "including" in the above cited passage from Order No. 05-584 has led to all sorts of mischief on the utilities' part. For example, Idaho Power's standard contract uses the phrase "at a minimum" when referring to the type of documentation it will require from a potential QF to demonstrate creditworthiness. The language in question is found at Section 4.1.6 of the Idaho Power standard contract:

> Provide Idaho Power with commercially reasonable representations and warranties and other documentation to determine the Seller's creditworthiness. <u>Such documentation would include, at a minimum,</u> that the Seller is current on existing debt obligations and has not been a debtor in a bankruptcy preceding (sic) within the preceding two years.

Emphasis provided.

Mr. Woodin's reading of the Commission's order at page 45 was quite the opposite. According to Mr. Woodin, the representations required by the

Commission should be considered the maximum that a utility may demand of a potential QF. According to Mr. Woodin, if the Commission felt that these representations were the minimal requirement they would have said so. The uncertainty caused by undefined terms that are apparently beyond of the scope of this Commission's reach is antithetical to the development of a healthy QF industry.[14]

THE UTILITIES OVERREACH ON DEFAULT SECURITY PROVISIONS

The Commission, in its Order, limited default security to recoupment of costs incurred by the utilities from future payments to the defaulting QF over a reasonable period of time. The Commission's clear pronouncement on this question notwithstanding, PacifiCorp's standard contract (at Section 11) contains provisions for letters of credit and/or cash escrow accounts as default security. The Commission did not provide for the posting of a letter of credit or cash escrow by QFs for default security provisoins. In fact, it appears from the following passage, that the Commission actively considered and rejected such devices which is evidenced by the first half of the first sentence in the passage from Order No. 05-584:

[14] Sherman/Simplot 110, at p. 6.

> <u>Although default security provided for in the form of a letter of credit or escrow deposit provides immediate recovery of costs incurred due to a QF's default,</u> we are persuaded that terms providing for future recovery over the course of a long term contract are reasonable. Consequently we adopt Staff's recommendation that standard contracts include a clause providing that, in the event that a QF defaults and the market prices to replace the contracted for energy exceed the contract price, future payments after the default period ends shall be commensurately reduced over a reasonable period of time to recoup the costs incurred by the utilities.

Emphasis provided. We also believe such a requirement is unnecessary and the utilities should be ordered to remove such terms from their standard contracts.

OPPORTUNITY TO CURE PROVISIONS ARE INCONSISTENT

Each utility has different contractual provisions for curing an event of default. PGE and PacifiCorp, have no provisions for an opportunity to cure for certain events of default. While the Commission has not specifically addressed this issue, it is important to the QF industry to have reasonable and consistent opportunity to cure provisions. Sherman/Simplot view the issue as one of commercial reasonableness and therefore endorse Idaho Power's approach - which allows a QF a "commercially reasonable" time in which to cure events of default. Depending on the event of default, PaciCorp and PGE both have clauses in their standard contracts that allow absolutely no opportunity to cure, which when compared to Idaho Power's approach, is completely inconsistent. It is illogical to suggest that two such disparate approaches to the same question can both be reasonable. The Commission is urged to adopt a consistent policy on this issue and a policy that is reasonable and not punitive. Allowing no opportunity to cure an event of default is punitive. Idaho Power's approach to this important issue is reasonable and appropriate for all utilities operating under the Commission's jurisdiction.

DELAY DAMAGES – MORE UTILITY GAMESMANSHIP

Staff's position on this issue is reasonable. That is, if the utility is resource surplus, then a QF's delay in coming on-line should not be an event of default and no penalties should be imposed. But this issue implicates another, more important question, and at the same time exposes a major inconsistency in the way avoided cost rates are set. For example, both PGE and PacifiCorp claim to be surplus for purposes of setting rates. If that is true, then failure of a QF to come on line is, by definition, not an event of default, because the utility doesn't need new sources of power during surplus periods. Yet the utilities are attempting to impose penalties against QFs for a delay in meeting contracted for on-line dates – even during times of surplus. That is inconsistent. In his direct testimony, Mr. Woodin testified at length about the need to eliminate resource surplus calculations when setting rates.[15] Yet, on the delay default issue, the utilities are playing a head- I-win and a tails-you-lose game. They claim to be resource sufficient when setting rates while at the same time claim to be harmed when a QF doesn't come on line during the surplus period. Logic dictates that delay default penalties should only be imposed if the avoided cost rates are set without a surplus period.

WEATHER SHOULD NOT BE AN EVENT OF DEFAULT

Sherman/Simplot agree with the Staff that weather related events should not lead to an event of default.[16] However, Staff's opposition[17] to including lack of wind or water as events of force majeure simply puts form over substance. Staff's MAG discussion[18] makes it clear that it does not believe that the lack of wind or water should be used to penalize the QF. Making the lack of wind or water an event of force majeure is a simple way of addressing this issue. Sherman/Simplot urge the Commission to so define force majeure in order to bring clarity on this issue for all parties.

Staff accepts the utilities' assertion that "force majeure events are limited to those that neither party could have anticipated." Staff/1 1000/55 – emphasis provided. However, it is simply not true that force majeure events are limited to

[15] Sherman/Simplot 105, at p. 5.
[16] Staff 1000, at p. 34.
[17] *Id.* at p. 55.
[18] *Id.* at p. 26.

just those events that are not anticipated. For example, the force majeure clause in Idaho Power's standard contract provides:

> "Force Majeure" or an "event of Force Majeure" means any cause beyond the control of the Seller or of Idaho Power which, despite the exercise of due diligence, such party is unable to prevent or overcome. Force Majeure includes, but is not limited to, acts of God, fire, flood, storms, wars, hostilities, civil strife, strikes and other labor disturbances, earthquakes, fires, lightning, epidemics, sabotage, or changes in law or regulation occurring after the Operation Date, which, by the exercise of reasonable foresight could not reasonably have been expected to avoid and by the exercise of due diligence, is shall be unable to overcome.

If an event of force majeure were "limited" to events that "neither party could have anticipated" then none of the events listed above (flood, fire, storms, lightning, etc.) could be an event of force majeure. Such a result would be absurd. Also contrary to Staff's assertion, events such as floods, storms, and lightning can be modeled and are, in fact, anticipated. It is only because the event in question is "*beyond the control*" of either party that it constitutes an event of force majeure. If a flood (too much water) constitutes an event of force majeur, then certainly a drought (too little water) may also constitute an event of force majeure. Both can be anticipated, both can be modeled, and both are beyond the control of the parties. Similarly, if a storm (too much wind) is an event of force majeure then a wind drought (too little wind) should also be an event of force majeure. Both can be anticipated, both can be modeled and, most importantly, both are beyond the control of either party.

SUMMARY

As with any complicated endeavor, the devil is in the details. The Commission is to be commended for bringing this case forward and its Staff should take pride in the progress made to date. As noted in the opening of this brief, utilities are reluctant to purchase power from QFs and therefore their response to this Commission's initiative should be viewed in that light. The continued failure of the Oregon utilities to host a robust QF industry is instructive and should be used as a guidepost by this Commission as it weighs the evidence and renders its decision.

As Mr. Woodin observed - ALL of the pieces of the puzzle must fit – if they do not then Oregon will remain doomed to a continued drought of QF development.

DATED this 20th day of March, 2006.

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By: ______________________________
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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on March 20, 2006, I served the foregoing via electronic mail and U.S. Mail parties of record in this docket:

Signed:____________________________
Peter Richardson