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' REPLY BRIEF**

I. INTRODUCTION

The Industrial Customers of Northwest Utilities ("ICNU") submits this Reply Brief requesting that the Public Utility Commission of Oregon ("Commission" or "OPUC") reject the proposals to make only minimal or overly conservative changes to the current rules regarding the requirements for investor-owned electric utility ("IOU" or "utility") purchases from Qualifying Facilities ("QFs"). As noted in ICNU's Opening Brief, there has been little or no QF development in Oregon for many years, and adopting only very minor modifications to the current rules will simply maintain the status quo. Instead, the Commission should adopt ICNU's proposals, which would1) require the utilities to offer standard contracts with a term up to the expected life of the QF facility to all non-wind QFs that have a nameplate capacity of up to 40 megawatts ("MWs"); and 2) require the utilities to file new tariffs including the specific guidelines regarding how

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avoided costs will be determined for QF contracts above the Commission-approved size threshold.

II. ARGUMENT

1. The Commission Should Not Continue the Status Quo of No QF Development by Making Only Minor Changes in the Rules Regarding Utility Purchases from QFs

The utilities, and to a lesser extent Staff, want to adopt only "measured and conservative" changes in the current rules. *E.g.*, Portland General Electric Company ("PGE") Brief at 10. According to the utilities, the Commission should adopt minimal changes because the current Commission rules and utility practices have not been shown to be barriers to QF development. PGE Brief at 7; PacifiCorp Brief at 2, 7-9. Similarly, Staff and the utilities oppose many meaningful changes to the current rules because of alleged risks of subsidies to QFs and potentialharm to ratepayers. PGE Brief at 13 -14; PacifiCorp Brief at 7-8; Idaho Power Company ("IPC") Brief at 8-10; Staff Brief at 4-5. The concerns raised by Staff and the utilities are largely unfounded, and the failure to modify the current Commission practices harm ratepayers by continuing to allow utilities to refuse to contract with cost-effective QF resources.

A. The Current Oregon Rules and Utility Actions Have Caused the Dearth of QF Development in Oregon

The utilities cannot dispute that there has been little to no meaningful QF development in Oregon for nearly two decades. Instead, the utilities argue that few changes are necessary because neither the Oregon rules nor the utilities are responsible for the lack of QF development. PacifiCorp Brief at 2; PGE Brief at 7. Throughout this

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proceeding, the utilities have denied that the Commission's QF rules and utility practices are to blame for the inability of QFs to enter into contracts with utilities, ascribing it instead to a variety of causes such as low power prices, high cost QF resources, energy intensive Oregon industries, or the lack of a need for resources in Oregon. *See*, *e.g.* PGE Brief at 7; PGE/100, Drennan-Kuns/24-25; PacifiCorp Brief at 2-3.

These arguments ignore the voluminous and often unrefuted evidence that QF development has not occurred in Oregon because: 1) the short contract lengths under the Oregon rules do not allow QF developers to obtain financing for their projects; and 2) QF developers are unable to negotiate fair and timely contracts with monopoly utilities that have financial incentives opposed to purchasing QF power. The fact is that low power prices and the lack of a need for resources have proven not to be significant factors limiting QF development, which is demonstrated by the fact that the utilities have failed to enter into QF contracts during periods of high power prices while they simultaneously have developed or acquired their own large resources.

No party directly contradicted the testimony of Staff and ICNU that requiring QFs to negotiate with the utilities has made it difficult, if not impossible, for QFs to enter into contracts with the utilities. *See* Staff/200, Schwartz/18-19; ICNU/100, Schoenbeck/2, 6, 9; ICNU/103, Schoenbeck/2, 6-7, 11-12. This evidence demonstrates that the negotiating process is flawed because the utilities have superior bargain positions and unnecessary delays often render projects uneconomic. *See* Staff/200, Schwartz/18-20; ICNU/100, Schoenbeck/6; ICNU/103, Schoenbeck/7, 11-12. Similarly, there is no dispute that utilities have financial incentives to favor their own resources. ICNU/100,

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Schoenbeck/6; Staff/100, Breen/3; Sherman/Direct, Reading/2. In addition, even PacifiCorp has admitted that longer term contracts are necessary because QFs cannot obtain financing under the current five-year contract term. PacifiCorp Brief at 4. Essentially, the evidence in this proceeding supports only one conclusion: that the lack of QF development is directly attributable to the Commission's rules and the utilities refusal to enter into QF contracts.

B. Avoided Cost Pricing Does Not Subsidize QF Developers

The argument in favor of making only minimal changes to the current QF rules is also based on an alleged concern that avoided cost pricing and standard contracts will result in subsidies to QF developers. PGE Brief at 13-14; PacifiCorp Brief at 7-8; IPC Brief at 10; Staff Brief at 4-5. For example, PacifiCorp asserts that "standard pricing results in an inherent subsidy" and the proposed changes to the current QF rules would simply create "a subsidy to stimulate QF development." PacifiCorp Brief at 7, 9. PGE also claims that proponents of changing the rules have an agenda to promote "societal goals or improve the potential financial returns to QFs." PGE Brief at 5. The majority of these alleged concerns regarding QF subsidies are red herrings designed to mask the utilities' real intentions of limiting or preventing QF development.

ICNU supports utility acquisition of the most cost-effective resources and opposes subsidies, whether to QF developers, renewable resources, or utility-contracted for or utility-owned resources. ICNU's proposed changes are designed to benefit ratepayers by diversifying the electric power supply and requiring the utilities to contract with cost-effective QF resources. As explained in ICNU's Opening Brief and testimony, standard pricing based on properly calculated avoided costs does not subsidize QF developers. ICNU Brief at 9-10. Avoided costs are projections of future costs that cannot perfectly match actual future costs. The risk thatavoided costs will differ from actual future costs exists for all resources, including utility owned resources; however, the risks associated with utility-owned resources have a much greater impact on ratepayers because of their significantly larger number, size, and duration.

The utilities also argue that pricing QF contracts based on the utility's avoided costs subsidizes QF developers because few QFs meet the characteristics of the proxy utility plant that is used to calculate avoided costs. PacifiCorp Brief at 7; PGE Brief at 13-14; *see* IPC Brief at 10. The utilities argue that QFs will be subsidized unless project-specific characteristics like plant dispatchability and location are used to lower the avoided costs paid to QF developers. PGE Brief at 14; PacifiCorp Brief at 11. However, the specific concerns raised by the utilities are relevant only for intermittent renewable resources and do not apply to typical cogeneration resources. Legitimate cogeneration facilities are matched to their thermal hosts, are located near load, and should not receive a subsidy if they are paid the utilities' avoided cost. *See* ICNU/103, Schoenbeck/12-13; ICNU/207-210. In addition, the project characteristics of many cogeneration facilities can result in additional savings by allowingthe utilities to avoid or postpone transmission and/or distribution investments.

More importantly, the utilities' true concern is not to avoid subsidies or ensure ratepayer neutrality, but to complicate and delay the negotiating process. *See* ICNU/100, Schoenbeck/6; ICNU/103, Schoenbeck/5, 11-12. To reduce the opportunities

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for the utilities to stonewall QFdevelopers with facilities larger than the Commission-established size threshold for standard offer contracts, the utilities should be required to include in their individual tariff filings a description of how project-specific characteristics will impact the avoided cost calculation. As explained in ICNU's Opening Brief, the current rules allow utilities to adjust the avoided cost calculation for projects above the size threshold by specific factors, including dispatchability, reliability, scheduling outages, and emergencies. ICNU Brief at 12-13. However, these factors are vague and ambiguous, and, in at least the recent past, no Oregon QF has been able to utilize them to successfully negotiate a non-standard contract. Id.; *see* Weyerhaeuser Brief at 14-17.

PGE appears to be opposed to including additional information in its tariffs, or developing specific requirements regarding the factors that can be considered in calculating avoided costs above the size threshold. *See* PGE Brief at 9, 15. PGE argues that a short, clean tariff is preferable to a voluminous tariff and that its tariff should merely reference the existing vague factors. PGE Brief at 15. The issue, however, is not volume versus brevity, but whether the current rules provide the necessary guidance and limit the utilities' ability to unnecessarily delay the negotiating process with QF developers. If project-specific characteristics are a real concern for the utilities, then the utilities should not be opposed to additional guidelines regarding how these factors impact the avoided cost calculation.

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2. Staff and the Utilities Have Not Demonstrated that Size Thresholds for Standard Contracts Should Be Limited to Less than 40 MWs

The issue of size thresholds for standard contracts raises a fundamental policy issue for the Commission: Does the Commission want to remove the fatal impediment of the utilities' stonewalling tactics for only small QF facilities? The utilities and Staff seek to remove this barrier to QF development for only small facilities, requiring medium and large QFs to continue the futile process of attempting to enter into timely and fair QF contracts with the Oregon utilities. Adopting the utilities two to-three MW size thresholds,[1/] or even Staff's 10 MW size threshold, will likely freeze out larger QFs, some of which could be the most efficient and beneficial resources available for Oregon ratepayers. For this reason, ICNU believes that, at a minimum, medium sized QFs up to 40 MWs should be permitted to enter into standard contracts with the utilities.

Staff and the utilities support small size thresholds for standard contracts based on arguments that the "intent of standard rates is to alleviate the disproportionate impact of transaction costs on . . . small projects." PacifiCorp Brief at 8-9; *see* PGE Brief at 6-7; Staff Brief at 7-8. Staff also supports its low 10 MW size threshold based on the fact that smaller QFs cannot sell their power at market. Staff Brief at 8. Although they did not directly address the issue in their rebuttal testimony, the utilities now dispute the evidence sponsored by ICNU and the QF developers that large QFs need standard

[1/] IPC currently supports a three MW size threshold for standard contracts. IPC Brief at 4. IPC does not explain or even acknowledge that it previously took the position that the size threshold should be 10 MWs. *E.g.*, ICNU/104, Schoenbeck/1.

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contracts because the "utilities can exploit asymmetries in information and bargaining power to thwart QF development." PacifiCorp Brief at 9; *see* PGE Brief at 5.

ICNU agrees that small QFs need access to standard contracts; however, the utilities and Staff have failed to justify why larger QFs do not also warrant standard contracts. For example, Staff has failed to explain why its concerns regarding QFs' ability to sell their power at market does not warrant a size threshold of at least 25 MWs, the size at which a QF could potentially sell at wholesale or participate in a utility bidding process. In addition, the utilities did not rebut the evidence sponsored by ICNU and Staff that large QF developers lack access to the information that is available to the utilities, are significantly harmed by the unnecessary delays in the negotiating process, and have been unable to enter into any contracts with utilities in nearly two decades. To ensure that utilities do not use the negotiating process to stonewall or refuse to enter into QF contracts, the Commission should adopt ICNU's proposed 40 MW size threshold.

3. A 15-Year Contract Term Discriminates Against QFs with Long-Term Financing Needs

Staff and the utilities support a 15-year contract term based on the argument that it balances the financing needs of developers with the risk of harm to ratepayers. Staff Brief at 4-5; PacifiCorp Brief at 4-5; PGE Brief at 10-11. PacifiCorp rejects ICNU's proposal that the contract length should match the investment needs of the QF facility because it claims a term of 15 to 20 years is adequate and QFs have the option to renew their contract once the initial contract expires. PacifiCorp Brief at 5. Although noting that it is unlikely to occur, Staff also suggests that QFs seeking longer contract

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terms should negotiate with the utility outside of the requirements of PURPA. *See* Staff Brief at 5.

The 15-year contract term appears superficially reasonable because it falls within the middle range of the financing needs of both utility-owned and QF facilities. For example, utility-owned or purchased resources have expected lives of five to 30 years while QFs have investment lives of five to 50 years. Staff/200, Schwartz/9; ICNU/100, Schoenbeck/9-10. However, the 15-year term is also an arbitrary compromise that unnecessarily discriminates against facilities with longer-term financing needs because those facilities are likely to be unable to obtain favorable financing. This includes many cogeneration, biomass, hydro, and wind facilities, and would have included the majority of QF facilities financed by the Department of Energy in the 1980s. ICNU Brief at 14-15. In addition, there is little to no evidence in the record that the option of renewing an initial contract or entering into a longer term contract outside of PURPA presents a realistic opportunity for QF facilities. In contrast, ICNU's proposal would allow all QF facilities to obtain financing and ensure that QFs with longer-term financing needs are treated comparably with long-term utility-owned resources.

III. CONCLUSION

ICNU respectfully requests that the Commission recognize that its current rules and utility practices have contributed to the complete lack of recent QF development. The Commission should adopt proposals that will foster the development of QFs without harming ratepayers. Expansion of the standard contract size threshold to 40 MWs is necessary for medium-sized QF facilities because they cannot sell their

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electricity at market or participate in utility requests for proposals and because the utilities have historicallyused the negotiating process to refuse to enter into contracts with QFs. The standard contract term should be extended to cover the economic life of the QF facility to allow all projects to obtain financing and to ensure comparability with utility-owned or purchased resources. Finally, the Commission should require all utilities to file new tariffs including, *inter alia*, specific guidelines regarding how avoided costs will be calculated for QF facilities above the Commission-established size threshold.

Dated this 27th day of January, 2005.

Respectfully submitted,

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