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September 30, 2011

Mr. David W. Danner
Executive Director and Secretary
Washington Utilities and Transportation Commission
1300 South Evergreen Park Drive S.W.
P.O. Box 47250
Olympia, WA 98504-7250

Subject: Docket No. UE-111405: Puget Sound Energy's Draft Request for Proposals from All Generation Sources (RFP) – Comments of TransAlta Corporation

Dear Mr. Danner:

TransAlta Corporation ("TransAlta") welcomes the opportunity to comment on Puget Sound Energy's ("PSE's") August 2011 Draft Request for Proposals from All Generation Sources ("RFP"). Overall TransAlta supports PSE's inclusion of a broad range of criteria in the RFP to be evaluated when comparing proposals to determine the lowest reasonable cost alternatives for generation resources. TransAlta's comments primarily address proper valuation of factors relating to public benefits associated with legislatively established public policies. In addition, the comments address two areas in general: the scope of the portfolio affected by generation resource decisions; and evaluation of risk.

Public Policies and Benefits

PSE is seeking additional power supply resources through its RFP process. WAC 480-107-035(2) requires that RFP ranking criteria include consideration of (among others) "public policies regarding resource preference adopted by Washington state or the federal government and environmental effects including those associated with resources that emit carbon dioxide." To meet this regulatory requirement, PSE should numerically quantify the benefits that a project provides through meeting the State's adopted resource preference policies as it evaluates alternatives in making resource acquisition decisions.

"Public Benefits" is one of the five categories in PSE's RFP evaluation criteria (RFP Exhibit A). The RFP criteria specified for Public Benefits, however, do not seem to include the specific "public policy" elements as directed by the rules; instead they are limited to environmental impacts, resource location and community support. Also, while indicating a "preference" for proposals with attributes in this general area, the RFP does not indicate how

this preference will be translated into a financially quantifiable value to enable the comparison of proposals from a lowest reasonable cost perspective. PSE must have some way to quantify the benefits arising from the public policy resource preferences adopted by the Legislature in order to meet the intent of WAC 480-107-035(2).

To illustrate how numerically quantifiable values can be attached to meeting such adopted resource preferences, we provide the following to illustrate how valuations could be ascribed for Washington state's most recent example of such an adopted public policy – the preference for coal transition power as found in Washington state Laws 2011, ch 180.

In adopting its preference for coal transition power, the Legislature specifically recognized the benefits this power (and the associated closure of a coal-fired facility) have in providing for:

- Implementation of the State's greenhouse gas reduction goals
- Stability and reliability of the electrical transmission grid
- Availability and affordability of power in the state
- Family-wage jobs and economic health in parts of the state
- Proper site cleanup and restoration
- Orderly transition to cleaner fuels.¹

The following sections discuss the quantification of each of these benefits in more detail.

Greenhouse gas reduction goals – as opposed to simply having low additional environmental impacts, coal transition power has been recognized by the Legislature and is being used by the State to meet its greenhouse gas reduction requirements set out in RCW 70.235.020. Absent transition power – and the associated closure of coal-fired facilities – to meet these requirements, the State would have to use some other mechanism, such as a carbon tax or utility fee, to achieve reductions in greenhouse gas emissions. In its 2011 IRP PSE shows scenarios for both a base case and a case that incorporates a cost for CO₂ mitigation.² The creation of coal transition power has moved the state away from a case where these costs would have to be incorporated into rates. The difference in these two price curves can be used approximate the value being created for PSE's ratepayers by the coal transition power. Alternatively this avoided cost could be approximated by looking at the costs of implementing a program such as that which is being implemented under California's Assembly Bill 32 on the energy mix serving PSE's customers.

¹ Laws 2011, ch 180, § 101.

² See, e.g., IRP at pages 4-20 to 4-21 (Summary Table of Scenario and Sensitivity Assumptions).

Stability and reliability of the electrical transmission grid – the locational benefits of power generation in the western portion of the state have been acknowledged in the legislation as well as various other studies and PSE’s IRP. Coal transition power provides system stability and reliability specifically benefiting PSE’s ratepayers by providing them with a secure source of power directly at PSE’s contracted transmission interconnection, protecting them against the risk of power interruptions when other transmission paths are constrained. This value can be estimated to be in the range of the avoided transmission cost that would be incurred to move power from Mid-C to this point of delivery.

Availability and affordability of power – the presence of coal transition power in the market provides a supply resource which helps to keep market prices lower for PSE’s ratepayers by impacting the cost of all power purchased. PSE’s IRP recognizes that the “No Northwest Coal” scenario would have higher costs for ratepayers, and also notes that if Centralia and Boardman “operations were significantly curtailed or shut down, PSE and its customers would be affected by the resulting impacts on market prices and regional transmission reliability.”³ The contribution of coal transition power to lower market power prices could be estimated by running a sensitivity comparing market price estimates arrived at by a fundamentals based market forecasting model in the presence and absence of Centralia.

Family wage jobs and economic health – coal transition power makes clearly identifiable contributions to family-wage jobs and economic health in parts of the state. These contributions include direct wages and the \$55 million required by the legislation for financial assistance to the affected community for energy efficiency and economic development; and for promising energy technologies. These benefits have been clearly recognized as part of the public policy initiative, and it is therefore in keeping with the requirements established by the state for the RFP evaluation process to include this value as part of the evaluation criteria. There are many potential methods to accomplish assigning a proportionate share of this value to PSE ratepayers, the simplest of which may be to allocate a proportion of the financial assistance proportionally to the coal transition contract.

Site cleanup and restoration – The evaluation process should expressly address risks and costs associated with project decommissioning. If PSE were to acquire a generating asset, PSE would be responsible for all decommissioning costs. By contrast, if PSE were to purchase power from another supplier, presumably the supplier would pay

³ IRP at 3-5; *see also* 1-8, 2-6, 5-40 and 5-41.

these costs.⁴ Proposals for PSE project acquisition would have an unfair advantage if decommissioning costs were not addressed. In any event, the RFP fails to require bidders to provide information about decommissioning and site restoration, and fails to recognize the value of sourcing power from suppliers with a proven track record of site remediation. Decommissioning costs should be required for proposed asset acquisitions and included as part of the total project cost calculation.

Orderly transition to cleaner fuels – If PSE were to acquire the peaking resources identified in its IRP,⁵ it would be making a very substantial financial commitment to new, fossil-fueled resources with efficiency levels below (and therefore emission levels higher than) that of combined-cycle resources, effectively guaranteeing 30 or more years of associated greenhouse gas emissions and locking in technologies that may soon be outmoded. Transition power promotes an orderly transition to cleaner fuels because it helps PSE keep its options open longer, so that it can at least defer the time when some of the new resource will be built, and may be able to use improved or non-fossil technologies when the capacity is finally needed. One method to estimate the value of this deferral would be to calculate a risk weighted estimate of potential carbon cost alternatives as described above, and the costs that would be attributable under these scenarios to simple cycle facilities.

General

In addition to the comments made above specifically in relation to the quantification of benefits resulting from achieving state policies, TransAlta offers these additional suggestions related to the need for additional quantification and increased scope and weighting that should be placed on other evaluation criteria identified in the RFP.

Concept of Portfolio

The RFP mentions consideration of how proposals fit into PSE's existing generation portfolio. This criterion should be broadened to include consideration of PSE's full asset and cost portfolio including not only generation but also PSE's existing and future needs for transmission resources and gas transportation and storage resources.

The benefits derived from utilizing existing assets such as transmission resources that PSE's ratepayers have already funded, and avoiding or delaying the need to incur future

⁴ The Legislature has squarely imposed on the supplier of transition power the obligation to prepare, finance and implement a detailed decommissioning and site restoration plan. Laws 2011, ch 180, § 201. Similar requirements apply to plants certified by the Energy Facility Site Evaluation Council. Ch. 463-72 WAC.

⁵ PSE's updated capacity need forecast at Table 2 calls for the addition of 1,065 MW of peaking capacity in 2014 and the further addition of 1,278 MW of peaking capacity in 2020. See document, "PSE's Capacity Need and Capacity Resource Characteristics," linked at <http://pse.com/aboutpse/EnergySupply/Pages/Acquiring-Energy.aspx> (updated September 9, 2011; last visited September 26, 2011).

costs for additional resources for gas and transmission are quantifiable and should be included in a measureable way in the comparison of alternative proposals.

Risk

In the descriptions of the criteria to be evaluated under the Risk Management section of evaluation criteria (Exhibit A), the RFP states, "*All other things being equal, PSE prefers operating projects first, projects under construction second, and development projects third*"; and, "*All other factors being equal, PSE prefers proposals that result in lower generation portfolio performance risk.*" A-5; A-6. Factors such as hydroelectric production variation, wind generation variability, fuel price volatility, carbon control costs, power market price volatility, and transmission congestion and costs are considered in this section. A-6.

There are significant and quantifiable differences in the risk levels and potential costs borne by ratepayers from proposals which differ in these areas. A key purpose of the IRP – RFP process is to address a wide range of risks with rigorous analysis. It is therefore inappropriate to consider them only in the context of a second tier analysis, being a tie breaker of sorts if all other things are held equal. The Commission's own rule underscores this point, providing that, "ranking criteria must recognize differences in relative amounts of risk ...[.]" WAC 480-107-035(2).

Companies commonly use discount rate comparisons to account for the additional risks incurred in taking on development and construction projects compared to the less risky alternative of relying on already operating assets. Well-grounded techniques exist in options theory to assess the value of risks such as resource variability and price volatility, which are commonly used to assess the costs that should reasonably be associated with alternatives of varying risk levels when comparing alternatives.

Recommendations

TransAlta respectfully requests that the Commission approve PSE's RFP subject to the following conditions:

1. The RFP's "public benefits" criteria should be expanded and revised to include recognition of public benefits legislatively established to be associated with the resource preferences of the State, including the policies set forth in Laws 2011, ch 180, § 101.

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2. PSE should refine its evaluation criteria as follows for purpose of arriving at a fair value adjusted price to enable comparison of proposals in order to establish the least cost reasonable alternative:
 - a. Include financial quantification of the legislatively established benefits the proposals provide through meeting the State's resource preference policies.
 - b. Expand the concept of portfolio to include consideration of PSE's full asset and cost portfolio including not only generation but also PSE's existing and future needs for transmission resources and gas transportation and storage resources.
 - c. Quantify different types and levels of risk to establish the value adjusted price; do not limit consideration of risk to proposals that are otherwise equal.
3. The RFP's request for information regarding proposals should include a request regarding the anticipated costs of and plans for project decommissioning, site restoration, and programs to be put in place to insure that these costs are covered.
4. The Commission would retain jurisdiction to effectuate the provisions of its order.

Thank you very much for your consideration of TransAlta's views. We hope that our comments can help establish an evaluation process that is as transparent and fair as is reasonably possible so that future generations of ratepayers may benefit from prudent resource acquisition decisions. Please direct any questions about these comments to Brenda Marshall at (360) 742-3113.

Very truly yours,

TRANSALTA CORPORATION

By 

Paul Taylor
President, TransAlta USA

Cc: Sheri Maynard, PSE (sheri.maynard@pse.com)
David Nightingale, Commission Staff (dnightin@utc.wa.gov)

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