

Agenda Date: October 26, 2005  
Item Number: A1

**Docket:** UE-051162  
Company Name: Puget Sound Energy, Inc.

Staff: Hank McIntosh, Regulatory Analyst  
Joelle Steward, Regulatory Analyst  
Yohannes Mariam, Regulatory Analyst

### **Recommendation**

Issue and order approving the filing of Puget Sound Energy in Docket UE-051162 (as revised ) and allowing the Company to publish its all-technology and Demand Side Management (DSM) Request for Proposals (RFP).

### **Background**

On July 29, 2005, Puget Sound Energy (PSE) filed its Draft Request for Proposals (RFP), pursuant to WAC 480.107.060(2)(a). The filing consists of two RFPs: an All-Source RFP that is for all generation sources and an Energy Efficiency RFP that is for electric and natural gas demand-side resources. Together, they are intended to satisfy and be consistent with WAC 480-107-060.

The RFPs seek resources, including demand-side resources, to meet energy and capacity needs over the period of 2006-2015. These resource needs were identified and preferences were guided by PSE's most recent Least Cost Plan. This Plan was filed May 2, 2005, and acknowledged by the Commission on August 29, 2005. Specifically, PSE's energy need is approximately 233 aMW in the 2006/2007 winter period increasing to over 1500 aMW by 2015. The capacity need is incremental to the average energy requirements and is estimated at 1000 MW in the 2006/2007 winter period, growing to 1600 MW by 2015.

The Commission published a Notice for Comment on August 10, 2005, requesting written comment to be filed at the Commission by September 28, 2005. Three parties filed comments with the Commission. All filed comments were specific to the All-Source RFP. On October 13, 2005, PSE filed its response to comments and submitted a number of proposed changes to the draft All-Source RFP.

## Discussion

### **All-Source RFP**

The Commission received comments on the All-Source RFP from Calpine Corporation, the Cogeneration Coalition of Washington and Pacific Power Marketing (PPM) Energy.

Calpine Corporation suggests the following:

- 1) PSE change its RFP to make PSE, not the seller, pay the expense of any fatal flaw analysis, if such analysis becomes necessary.
- 2) An independent evaluator be used to report on the solicitation process and to supervise the resulting bids.
- 3) The requirement for posting a credit instrument (if necessary) be bi-lateral, and not the sole obligation of the seller.
- 4) No allowance for the possible existence of imputed debt be allowed in the evaluation process.
- 5) The requirement that sellers produce confidential business and financial data to the buyer for an evaluation under FIN 46<sup>1</sup>, be made optional (since, they assert, the requirement under FIN 46 is merely the existence of an *attempt* by the buyer to elicit this data, not a requirement.)
- 6) Calpine further calls for the WUTC to convene a proceeding to determine the special impacts on costs and benefits that purchase power agreements (PPAs) bring to power utility customers.

The Cogeneration Coalition of Washington has three recommendations for the All-Source RFP:

- 1) PSE should include a detailed quantification of environmental benefits of cogeneration resources.

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<sup>1</sup> FIN46 is for control of variable interest entities. A variable interest entity, or VIE, is a corporation, partnership, trust, or any other legal structure used for business purposes that either does not have equity investors with adequate decision making ability or has equity investors that do not provide sufficient financial resources for the entity to support its activities.

- 2) PSE should provide more information that a respondent may use to assess development risks for new projects and transmission benefits from existing facilities.
- 3) A quantification of the benefits cogeneration brings to the local economies (distinct from PSE's service territory).

PPM Energy, a subsidiary of ScottishPower, Inc., requests that:

- 1) The evaluation of bids explicitly recognize its understanding of the greater value in existing resources over resources under development.
- 2) PSE fully consider bids from sellers offering resources under their control but not ownership.
- 3) PSE change from 2 to 3 days the requirement for adequate assurance in its Definitive Credit Agreements.
- 4) PSE change language in the section on "Investment Grade Respondents" making credit adjustments in financial covenants bilateral rather than applying only to the seller.
- 5) The definition of "investment Grade" in the Prototype Power Purchase Agreement cover corporate credit ratings from S&P or Moody's and not a simple Long Term Debt rating, which they assert would alleviate the need that the seller's guarantor meet the earnings-to-interest ratio test.
- 6) PSE remove from the requirements or substitute a guaranty from a credit worthy entity instead of a Letter Of Credit for drawing upon if the seller defaults its obligation to pay delay payments.
- 7) The use and calculation of imputed debt be made not by PSE but by the WUTC, to ensure fair treatment of both PSE and sellers.

Staff attended pre-filing meetings with PSE on June 21 and 22, 2005, as well as the post-filing informational outreach meeting for potential bidders August 18, 2005. On October 5, 2005, Staff met with PSE to discuss their responses to public comment as well as continuing results of their 2004 solicitation. On October 14, 2005, PSE filed a formal reply to comments and revisions to their draft RFP with the WUTC.

The Company proposes the following revisions to the draft All Source RFP:

- 1) PSE has changed the language at page 3 to clarify that they encourage small scale as well as large scale projects to participate.
- 2) PSE has expanded its request for proposed exchanges during heavy load hours to include proposals for 7 day 16 hours (7x16), 7 day 24 hour (7x24), and six day, 16 hour (6x16) products.
- 3) PSE has replaced description of its preference for proposals near in time with language that expresses preference for energy and/or capacity in time frames consistent with its needs.
- 4) PSE has clarified language that its view of risks of environmental regulation and taxes includes specific consideration of greenhouse gas issues.
- 5) PSE has added ramp rates for cold, warm, and hot starts as well as associated fuel estimates to the list of items required for unit startup information.

Staff has reviewed PSE's July 29th filing and its responses to the comments filed October 13th. Staff believes that the revisions are reasonable and in the public interest. Generally, Staff believes that the goal of the RFP is to ultimately produce offerings that have the greatest ratepayer advantages of cost and risk minimization. The standard of non-discrimination and the presence of unconstrained bidding allows for suitable fairness for bidders as well as protection for ratepayers. It is also the closest substitute to a market process available for non-commodity acquisition.

In particular, Staff points out that the risks and costs of providing information to buyers is normally the burden of sellers and that sellers are not compelled to bid on this RFP. The impacts of the cost of capital and the cost effects on operations stemming from a firm's credit status cannot be hidden from view of managers and later used to hold them accountable. The issue of imputed debt is of small consequence for large companies with robust financial ratings, but it is not so for those in lesser circumstances. The particular calculations PSE uses in each bid's evaluation will be reviewed at prudence determination. It should be noted that recent experience has demonstrated that PSE has screened out more bids for the practical defects of deliverability to a specific point in a given time frame and for credit and business credibility concerns than for imputed debt reasons. Further, PSE has substantial PPA contract power in its portfolio and has recently added a short-term PPA to its portfolio. There is no current evidence known to Staff that competitive PPA bidders are capriciously rejected due to

the imputed debt consideration. Finally, WAC 480-107-070(3) requires consideration of financing risk in bid evaluations.

As a general point, Staff observes that criticism of RFPs for requiring too much data must be viewed soberly. Since the Company is ultimately the decision maker and must assess the risk of supply, we do not believe the Commission should undermine its ability to get the information required for the Company's analysis, without very clear and purposeful reasons, which we do not find here. Otherwise, regulators cannot hold the Company accountable for its supply decisions. Fundamentally, the goal of regulation is not to minimize rates by arbitrarily increasing stockholder risk, nor is it to ease the management's burden of managing operational and financial risk. Its goals include avoiding an increase in utility risk without concrete, systematic, long-term benefits (such as cost reduction and stability) for captive ratepayers. Wholesale sellers can find other markets, but our ratepayers have only one power provider.

### **Energy Efficiency RFP**

PSE's Energy Efficiency RFP seeks proposals for electric and natural gas energy efficiency resources, which will help meet its energy resource needs. PSE will consider proposals for any energy efficiency projects that meet the general requirements of the solicitation, e.g., a project must produce savings over more than 5 years and it must be able to reliably measure the savings. In addition to the open solicitation, it is targeting specific types of projects to enhance their current portfolio of programs.

No party submitted written comment to the Commission on the Energy Efficiency RFP and the Company has not proposed any revisions to the draft. Staff has reviewed the draft RFP and believes that it is reasonable and in the public interest. The solicitation is open enough to allow market actors to identify additional opportunities the Company may not have considered. The inclusion of targeted areas, however, was a request by bidders in the last RFP and will help some potential bidders focus their efforts and resources. We are hopeful that this RFP will provide additional market information on price and program design that will supplement the supply curves the Company recently prepared for its least cost plan. Of particular note, PSE has included natural gas projects in this RFP for the first time, even though natural gas is outside the scope of

the Chapter 107 WAC. We praise this decision because we believe that this is a highly opportune time to seek natural gas efficiency projects in light of recent cost increases.

Summary

Staff has reviewed the revised RFPs and believes that PSE's revisions reflect a reasonable consideration of public comment. The contents of the RFP document contain the required elements as described in Chapter 107 WAC. Staff concludes that these RFPs comply with the rule and are in the public interest.

Conclusion:

Approve the filing (as revised by Company) as being in the public interest pursuant to WAC 480-107-060 and allow Puget Sound Energy to publish its All-Source and Energy Efficiency RFPs.