

**BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH**

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In the Matter of the Application of )  
PACIFICORP for a Certificate of )  
Convenience and Necessity Authorizing )  
Construction of the Lake Side Power Project)

Docket No. 04-035-\_\_\_\_

**DIRECT TESTIMONY OF  
DONALD N. FURMAN**

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**MAY 2004**

1 **Q. Please state your name, business address and position with PacifiCorp.**

2 A. My name is Donald N. Furman. My business address is 825 NE Multnomah, Suite 2000,  
3 Portland, Oregon 97232.

4 **Qualifications**

5 **Q. What is your current position at PacifiCorp (the Company)?**

6 A. My present position is Senior Vice President, Regulation and External Affairs.

7 **Q. Briefly describe your educational and professional background.**

8 A. I hold a Bachelor of Arts degree in economics from Northwestern University and a Juris  
9 Doctorate degree from Lewis and Clark Law School. Before assuming my present  
10 position with PacifiCorp, I served as Vice President of Transmission, Vice President of  
11 Domestic Business Development, and President of the Company's unregulated power  
12 marketing subsidiary.

13 **Q. What are your responsibilities as Senior Vice President, Regulation and External  
14 Affairs?**

15 A. I am responsible for all of the Company's regulatory and governmental relationships. I  
16 oversee all regulatory matters before six state utility commissions and the Federal Energy  
17 Regulatory Commission. I am responsible for all of the Company's political activities at  
18 both the state and federal level.

19 **Q. Have you previously testified before the Utah Public Service Commission  
20 (Commission)?**

21 A. Yes. Most recently, I appeared in the Docket No. 03-035-29, the certificate of public  
22 convenience and necessity proceeding for the Currant Creek power plant.

1 **Purpose and Summary of Testimony**

2 **Q. What is the purpose of your testimony?**

3 A. The Company's application for a certificate of public convenience and necessity  
4 authorizing construction of the Lake Side Power Project is the subject of this proceeding.  
5 The purpose of my testimony is to provide an overview of the resource acquisition  
6 process which has culminated in PacifiCorp's decision to select the Lake Side Power  
7 Project to provide the additional supply-side resources that will be needed to serve  
8 customers by the summer of 2007. Specifically, I will explain that the decision to acquire  
9 the Lake Side Power Project is consistent with PacifiCorp's 2003 Integrated Resource  
10 Plan (IRP), the updates to the IRP and Request for Proposal (RFP) 2003A. Throughout  
11 the process, the Company's goal has been to find the option that provides customers and  
12 PacifiCorp with the best cost/risk alternative. I will explain that in seeking to accomplish  
13 this goal PacifiCorp had no predetermined notion or bias towards any type of resource,  
14 whether it be self-build or a power purchase agreement (PPA), but engaged in earnest and  
15 good faith consideration and evaluation of all proposals. I will briefly summarize the bid  
16 evaluation process and examine the key factors that ultimately drove the decision to  
17 select the Lake Side Power Project. Finally, I will introduce the other witnesses who  
18 have filed direct testimony in support of this application.

19 **Consistency with established IRP and RFP**

20 **Q. Is the construction of the Lake Side Power Project consistent with PacifiCorp's**  
21 **resource needs as identified in its 2003 IRP?**

22 A. Yes. The resource acquisition process that led to the selection of the Lake Side Power  
23 Project began with the compilation of an integrated resource plan that has been

1 acknowledged by this Commission and widely praised and emulated. The 2003 IRP  
2 document includes a detailed description of the Company's system and how it operates.  
3 The IRP was created in a public process open to all interested parties and which resulted  
4 in many months worth of analysis that the Company did specifically to address  
5 stakeholder issues. These additional analyses and perspectives substantially strengthened  
6 the resulting IRP document.

7 **Q. What specific needs were identified in the 2003 IRP that bear on this proceeding?**

8 A. As discussed by Melissa Seymour, the 2003 IRP filed in January 2003 found a need for  
9 substantial new resources, particularly in the East portion of PacifiCorp's system, which  
10 includes Utah. Because of transmission constraints, the East portion of the system  
11 requires more in-state physical resources to fulfill the Company's obligation to serve  
12 load. These constraints limit imports from other electrical systems and create a need to  
13 buy or build additional regional capacity. More recent load forecasts indicate an even  
14 larger resource gap for the East than was projected in the 2003 IRP.

15 **Q. What actions are proposed in the 2003 IRP to meet the identified resource**  
16 **requirements?**

17 A. The IRP set forth an action plan consisting of twenty-eight recommended actions to  
18 implement the plan. Action Item No. 2 called for additional supply-side resources to be  
19 added in the East portion of PacifiCorp's system in Fiscal Year 2008 (April 2007-March  
20 2008). However, since the East portion of the Company's system typically reaches peak  
21 load during the summer, it is critical that the new resource be available by that time  
22 (summer of 2007). Thus, IRP Action Item No. 2, which called for approximately 570

1 MW of base load resource, became the underlying purpose for establishing the 2007 bid  
2 category in RFP 2003A.

3 **Q. Please summarize the content of RFP 2003A.**

4 A. Mark Tallman provides an explanation of the RFP 2003A process, and I won't repeat that  
5 discussion here. However, described in the most general terms, the RFP solicited supply-  
6 side resources in three bid categories: (1) "SuperPeak; (2) "Peaker"; and "2007  
7 Resource". The Company received no acceptable bids in he SuperPeak bid category.  
8 The results of the Peaker category produced the Currant Creek Project (Docket No. 03-  
9 035-29) as the best cost/risk alternative, and the 2007 Resource is the subject of this  
10 proceeding.

#### 11 **Implementation and Administration of the RFP Process**

12 **Q. How would you characterize PacifiCorp's administration of the RFP bidding**  
13 **process for the 2007 Resource?**

14 A. I believe the process was rigorous, neutral and fair. That said, I must concede as I have  
15 on previous occasions, that while the RFP generated a large number of respondents, the  
16 pool of experienced and qualified bidders was decimated by the outfall of the energy  
17 crisis and the collapse of Enron. Even the major players who survived to submit bids  
18 were financially weakened. This is not the fault of the RFP process, nor of the bidders,  
19 but it must be taken into account in assessing the results of the bid evaluations.

20 **Q. Was the competitive bidding process for the 2007 Resource subject to independent**  
21 **third party review and evaluation?**

22 A. Yes. Subject to a stipulation between PacifiCorp and various parties to Docket No. 03-  
23 035-03, Navigant Consulting, Inc. (Navigant) was engaged as an independent consultant

1 to evaluate the bids out of the presence of the Company. In this regard, Navigant's role  
2 was identical to that which it had played in the recently concluded Currant Creek  
3 proceeding.

4 **Q. Did the bid evaluation process for the 2007 Resource follow the same procedures**  
5 **used to evaluate the bids in the other RFP category?**

6 A. Yes. The same review process that was exhaustively reviewed by the Commission for  
7 the selection of the Currant Creek facility was also followed in evaluating the bids in the  
8 2007 category.

9 **Q. What was the Company's goal in administering the RFP process?**

10 A. PacifiCorp's goal in administering the RFP process was to find the best cost/risk  
11 alternative for customers.

12 **Q. In evaluating the bids for the 2007 Resource, did PacifiCorp have a predisposition**  
13 **to favor a turn-key proposal (wherein the Company would own the facility) over**  
14 **some form of purchased power agreement (PPA)?**

15 A. No. The Company had no predetermined notion or bias towards any type of resource,  
16 whether self build, turn-key or PPA, but engaged in earnest and good faith consideration  
17 and evaluation of all proposals.

18 **Q. Isn't it true that PacifiCorp has a vested interest in owning generating facilities**  
19 **rather than purchasing power from third parties because the Company only earns a**  
20 **profit when it invests in capital projects and places those projects into rate base?**

21 A. No. The idea that utilities are focused on maximizing rate base is a persistent  
22 misconception that betrays a fundamental misunderstanding of the way in which  
23 regulated utilities provide value for their shareholders. In the course of my

1 responsibilities for the Company, I participate in making recommendations on matters  
2 presented to the PacifiCorp Board of Directors, including the selection of the 2007  
3 Resource. I can say categorically that the management of PacifiCorp does not evaluate  
4 the merits of a proposed resource acquisition based on whether the Company will own  
5 the asset or purchase the output of the asset from a third party. Rather all decisions are  
6 evaluated based on the prospects for achieving full recovery of the expenditure.  
7 Disallowance is always the key consideration, and it is never the need to increase rate  
8 base.

9 **Q. Why is the prospect for disallowance so much more important than the size of rate**  
10 **base in PacifiCorp's decision-making process?**

11 A. The fact is that disallowances directly affect the return that investors earn while the size  
12 of rate base does not. When the Commission finds that the Company invested money  
13 imprudently and disallows recovery of that investment from rates, the Company's return  
14 on that investment is reduced by the amount of the disallowance. Since the investment  
15 has already been made, the result is an earned return on equity that is less than the  
16 allowed return on equity. Given that the allowed return is set with reference to the  
17 desired return demanded by investors in the marketplace, the stock price will suffer when  
18 earned returns lag those allowed, particularly if the lag is associated with a regulatory  
19 disallowance. Investment analysts with whom I converse regularly are greatly concerned  
20 with disallowances and the steps that PacifiCorp takes to ensure that it does not make  
21 expenditures that our commissions would deem to be imprudent. Therefore, it should  
22 come as no surprise that these issues get management's attention.

1 **Q. Doesn't an increasing rate base provide higher returns for PacifiCorp investors,**  
2 **resulting in higher stock prices?**

3 A. Absolutely not. I have never heard a stock analyst express concern over lack of growth  
4 in PacifiCorp's rate base. This is a totally rational response because growth in rate base  
5 does nothing to increase return to shareholders. It is certainly true that the Company's  
6 total earnings are a function of return on the rate base. Total return on rate base is part of  
7 the revenue requirement calculation, and the revenues the Commission allows PacifiCorp  
8 to recover include a return on rate base. However, increases in rate base must also be  
9 financed. This financing is accomplished by issuing debt and equity. If we add to rate  
10 base by issuing new equity, then earnings per share will not rise, assuming a constant  
11 ratio of debt to equity is maintained. Finally, it should be noted that PacifiCorp's rate  
12 base is already growing steadily as a result of necessary infrastructure improvements,  
13 without adding any new generation facilities.

#### 14 **Evaluation of bids for the 2007 Resource**

15 **Q. What comments do you have on the bid evaluation process for the 2007 Resource?**

16 A. It is not my intention to repeat the thorough description of the bid evaluation process  
17 which is provided in Mark Tallman's testimony. However, I would like to comment on  
18 the criteria used to compare the two finalist bids against one another, criteria which  
19 ultimately resulted in the selection of the Lake Side Power Project.

20 **Q. Would you briefly summarize the process explained in Mr. Tallman's testimony**  
21 **which resulted in the identification of the two finalist bids for the 2007 Resource?**

22 A. The first step in this process was the selection of the benchmark resource, or Next Best  
23 Alternative (NBA), that the bids in the 2007 category would be compared against. It was

1 determined that the NBA for the 2007 Resource would be an expansion of the Currant  
2 Creek Project. As a result of the bid solicitation, fifty-three specific offers were received,  
3 presenting a wide range of proposals. Twenty of these offers from nine individual  
4 companies were short-listed for consideration. When these bids were compared against  
5 the NBA, the list of companies was reduced to three—comprising of bids number 213,  
6 number 922 and number 493. Ultimately, bid number 922 was rejected after it was  
7 determined that the project imposed an unreasonable amount of risk on PacifiCorp  
8 customers, given the critical need for new resources to be available by the summer of  
9 2007. The two remaining options were bid number 493 (Summit) and bid number 213.

10 **Q. Please describe the nature of the two remaining competing bids.**

11 A. Summit Power, via Summit Vineyard, LLC (Summit), submitted a bid to develop,  
12 construct, and transfer, upon completion, the ownership of the power plant (Lake Side  
13 Power Project) to PacifiCorp (Turnkey). Summit would enter into an EPC contract with  
14 Siemens Westinghouse Power Corporation (Siemens Power) to construct the resource.  
15 Bid number 213 was a tolling services agreement (TSA) where PacifiCorp would supply  
16 the gas to be converted to electricity. A TSA can be distinguished from a traditional  
17 power purchase agreement in that a PPA typically requires the seller to bear the fuel  
18 procurement risk.

19 **Q. What sites were proposed for the two bids?**

20 A. Both bidders proposed to use the same site for the location of their prospective resources.  
21 This site is located at Geneva Steel and is in proximity to end-use loads and PacifiCorp's  
22 345 kV and 138 kV transmission systems.

1 **Q. What were the primary considerations in evaluating the two proposals?**

2 A. The overriding consideration was the need to have a physical asset available to serve  
3 increasing load in 2007. Since PacifiCorp's ability to get power into the East portion of  
4 its system is constrained, the availability of a physical resource within the Utah bubble is  
5 absolutely vital to serve load in 2007. There is no margin for error. The other factor that  
6 weighed heavily in evaluating the final two bids was economics. Naturally, a comparison  
7 of the economic performance of the two proposals was an important consideration. In  
8 this case, the issues raised by other parties in the Currant Creek proceeding (Docket No.  
9 03-035-38) relating to real levelization are not applicable in comparing the build and own  
10 option against the TSA arrangement. This was so because the bidder for bid number 213  
11 offered the Company an option to extend a 20-year TSA for an additional 15 years  
12 beyond the initial term. The economic analysis assumed the Company would exercise  
13 this option and end up with a 35-year TSA agreement. In addition to the 35-year analysis  
14 period, the economic analysis for bid number 213 also reflected the fact that this bidder  
15 ultimately indicated its intent to accept, but not to fully collateralize, the risk of future  
16 expenses associated with carbon dioxide (CO<sub>2</sub>) liability during the first 20 years of the  
17 proposed transaction. The bid number 213 analysis also reflected the additional costs  
18 associated with its incremental debt impact on the Company. This cost is not associated  
19 with the Lake Side Power Project because the Company will directly issue debt  
20 associated with the purchase of that facility. The final step in the evaluation was to  
21 consider the relative economics of the two bid proposals in light of their respective credit  
22 risk, CO<sub>2</sub> liability and schedule risk, which may impact the ability of the bidder to deliver  
23 the required physical resource in 2007.

1 **Q. What was the result of the economic analysis of the Lake Side Power Project?**

2 A. The Lake Side Power Project had economics that evaluated to be \$2.90/kW-month if a  
3 second gas connection was included and \$3.04/kW-month without the second connection.  
4 In addition, as discussed in the testimony of Mr. Tallman, it does not appear that a  
5 secondary connection to Questar LDC will provide commercial advantage. Given this  
6 and the fact that the Lake Side Power Project is backed by a strong, creditworthy entity,  
7 the Company believes that \$3.04/kW-month is the appropriate economic evaluation for  
8 the Lake Side Power Project.

9 **Q. What was the result of the economic analysis for the bidder for bid number 213?**

10 A. Bid number 213, with a term of 35 years and assuming an engineer, procure, construct  
11 (EPC) wrapped contract with a single entity to construct the resource, had economics that  
12 evaluated to, without including the CO<sub>2</sub> liability assumptions, \$0.77/kw-month. the  
13 proposal from the bidder for bid number 213 had, with the CO<sub>2</sub> liability assumptions  
14 included and assuming no delay in performance, economics that evaluated to be  
15 \$3.07/kw-month. However, due to the poor credit rating of the bidder for bid number  
16 213, the Company considered the risk of delay associated with default. If such a delay  
17 resulted in the resource not being available to meet the critical 2007 summer time period,  
18 the economics change such that if a 2-month delay ensued, then the economic evaluation  
19 fell from \$3.07/kW-month to \$2.90/kW-month. With a 4-month delay, the economics  
20 fell to \$2.65/kW-month. Given the size of the resource, and using the 4-month delay  
21 scenario, a 25 percent scarcity premium in the market would result in economics of  
22 \$2.47/kW-month. In addition, in analyzing these economics, the Company recognized

1 that it was assuming that it would be possible to import significant amounts of power into  
2 the constrained Utah market.

3 **Q. So, would you agree that the CO<sub>2</sub> liability is a major factor in evaluating the**  
4 **economics of the Lake Side Power Project and bid number 213?**

5 A. Yes, it is a key consideration. As I mentioned previously, the economics of bid  
6 number 213 benefit significantly from including the CO<sub>2</sub> liability assumptions.  
7 However, PacifiCorp has serious concerns that the entity that provided bid number 213  
8 will not have the future financial capacity to make good on its commitment to absorb  
9 CO<sub>2</sub> risks. The total dollar value associated with the CO<sub>2</sub> liability assumption by the  
10 bidder is more than \$600 million in nominal terms. In fact, concerns about the future  
11 financial stability of the entity providing bid number 213 do more than just cast doubt on  
12 the validity of the economic comparison. These credit concerns call into question the  
13 ability of this bidder to meet the threshold evaluation criteria, which is the ability to  
14 deliver the required physical resource in 2007. Obviously, any delay in resource  
15 availability would further reduce the economic value of bid number 213.

16 **Q. Is it your testimony that the delivery risk associated with these two resource**  
17 **proposals was a material consideration with respect to the Company's final**  
18 **decision?**

19 A. Yes. As I explained earlier, PacifiCorp believes that there is no margin for error with  
20 respect to the ability to deliver the physical asset needed to serve load in 2007. When  
21 presented with two resource proposals that have, including CO<sub>2</sub> liability assumptions, the  
22 appearance of being economically comparable, the Company must inevitably choose the  
23 alternative that provides the greatest certainty of resource availability.

1 **Q. Please describe the Lake Side Power Project.**

2 A. The Lake Side Power Project is a 534 MW combined cycle combustion turbine (CCCT).  
3 The Lake Side Power Project will be developed by Summit Power, via Summit Vineyard,  
4 LLC (Summit). Summit will enter into an EPC contract with Siemens Westinghouse  
5 Power Corporation (Siemens Power) to construct the resource. Summit and Siemens  
6 Power have worked extensively together on a variety of CCCT projects and have  
7 delivered these new resources on time and per agreement. Siemens Power will guarantee  
8 their work under the EPC.

9 **Q. Is PacifiCorp confident about Summit's financial stability and credit worthiness as**  
10 **measured by its ability to complete the Lake Side Power Project by the summer of**  
11 **2007?**

12 A. Yes, without question. Summit and Siemens Power have built 12 plants together over the  
13 past six years. Summit, founded in 1989, has a proven track record of bringing its  
14 projects from inception through completion, on time and within budget, with all operating  
15 plants performing up to or exceeding expectations. Siemens Power is well-known as an  
16 international power plant construction company, with more than 655,000 megawatts of  
17 installed capacity worldwide.

18 **Q. How does PacifiCorp assess the credit worthiness of the entity providing bid**  
19 **number 213?**

20 A. An assessment of the relative credit worthiness of Summit/Siemens Westinghouse and  
21 the entity providing bid number 213 is provided in the testimony of Richard Ito. Mr. Ito  
22 observes that the company providing bid number 213 is a non-investment grade entity  
23 with an unsecured debt rating of "Caa1" from Moody's. In contrast, the Summit proposal

1 (the Lake Side Power Project) is guaranteed by an investment grade rated entity (Siemens  
2 Power) with an “A2” rating from Moody’s. According to Moody’s, as a “Caa1” rated  
3 entity, the bidder submitting bid number 213 has a 48 percent to 64 percent chance of  
4 defaulting on its debt within the next three years. As an “A2” rated company, Siemens  
5 Power has a 0.23 percent to 1.74 percent chance of defaulting during the same period.  
6 Mr. Ito also points out that in addition to the financial risk, the transaction proposed in  
7 bid number 213 would have encompassed numerous separate agreements to document  
8 the rights and obligations of both counterparties whereas the Summit proposal includes  
9 fewer contracts.

10 **Q. What factors drove the final choice of the Summit proposal over the alternative?**

11 A. One of the primary objectives of RFP 2003A was to obtain resources with the best  
12 cost/risk balance. Both the Summit proposal and bid number 213 were presented to  
13 PacifiCorp’s Senior Management, including myself, for review. We weighed the costs  
14 and risk of each alternative carefully, and the Senior Officers of the Company determined  
15 that the Lake Side Power Project displayed the most prudent balance between cost and  
16 risk. Key in this determination was PacifiCorp’s obligation to serve and the need to have  
17 the resource in place by the summer of 2007 in order to meet the demand predicted by the  
18 IRP. Ultimately, the risk of delay resulting from a credit event or schedule risk and  
19 concern over the ability of the bidder for bid number 213 to perform on its acceptance of  
20 the CO<sub>2</sub> liability, given its credit rating, was found to impose unacceptable risks on  
21 customers.

1 **Q. Do you have any final comments on the competitive resource acquisition process**  
2 **undertaken by PacifiCorp?**

3 A. Yes. PacifiCorp continues to support the acquisition of new resources through  
4 competitive bidding processes. However, it is becoming increasingly clear that the  
5 selection of the successful bidder will always require the Company to make difficult and  
6 potentially controversial decisions. To some degree, these decisions will require making  
7 assumptions about the future for which no one can claim to have perfect knowledge. In  
8 performing its evaluations, PacifiCorp follows a process of gathering the best information  
9 available and subjecting that information to scrutiny by talented and knowledgeable  
10 people. Part of that scrutiny necessarily involves risk assessment. The independent  
11 power development industry is currently distressed and the entity offering bid  
12 number 213 is especially so. These are factors that cannot be ignored. The entire bid  
13 evaluation process operates within a framework that must recognize the Company's  
14 obligation to serve its customers and to serve them safely, reliably and efficiently. We  
15 are confident that we have made the right choice in selecting the Lake Side Power Project  
16 as the 2007 Resource—not necessarily the easy or popular choice, but the right choice for  
17 our customers.

18 **Q. What action is PacifiCorp asking the Commission to take in this proceeding?**

19 A. PacifiCorp asks the Commission to determine that there is a need for a resource in 2007,  
20 that the Lake Side Power Project meets that need and that the Lake Side Power Project is  
21 the best cost/risk alternative for customers. For all these reasons, the Company asks the  
22 Commission to issue a certificate of convenience and necessity for the Lake Side Power  
23 Project.

1 **Introduction of Witnesses**

2 **Q. Please introduce the other witnesses who have submitted direct testimony in support**  
3 **of the Company's application in this proceeding.**

4 A. The following witnesses have submitted direct testimony supporting the issuance of a  
5 certificate of convenience and necessity for the Lake Side Power Project.

6 Mark R. Tallman, Managing Director of Trading & Origination for PacifiCorp,  
7 will describe how the two finalist bids received for the 2007 Resource compared against  
8 one another and against the benchmark resource (expansion of Currant Creek).

9 Richard Y. Ito, Vice President of U.S. Energy Risk Management for PacifiCorp,  
10 will describe how the final bids negotiated for the 2007 Resource were evaluated from a  
11 risk management perspective.

12 Melissa A. Seymour, Manager of Planning and Financial Analysis for  
13 PacifiCorp, will discuss PacifiCorp's resource needs as identified in the 2003 IRP, the  
14 update to the 2003 IRP, and the public process surrounding both filings.

15 Bruce N. Williams, Treasurer of PacifiCorp, describes in general terms how the  
16 Company will fund acquisition of the Lake Side Power Project.

17 Howard Friedman, a Principle with Navigant Consulting, Inc., will address the  
18 central components of the RFP 2003-A process used by PacifiCorp to identify the  
19 resource with the best cost/risk balance. Mr. Friedman will also lay out Navigant's role  
20 in independently monitoring this process to ensure that PacifiCorp's review and selection  
21 process was consistent, fair and reasonable.

22 **Q. Does this conclude your direct testimony?**

23 A. Yes.