

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application of)
PACIFICORP for a Certificate of)
Convenience and Necessity Authorizing) Docket No. 04-035-30
Construction of the Lake Side)
Power Project)

REBUTTAL TESTIMONY OF HOWARD FRIEDMAN

October 15, 2004

1 **I. INTRODUCTION**

2 **Q. Please state your name, business name, and business address.**

3 A. My name is Howard Friedman. I am employed by Navigant Consulting Inc as an
4 Associate Director. My business address is 175 West Jackson, Suite 500,
5 Chicago, Illinois 60604.

6 **Q. Have you previously testified in this proceeding?**

7 A. Yes. I submitted pre-filed direct testimony on May 28, 2004.

8 **Q. What is the purpose of your rebuttal testimony?**

9 A. The purpose of my rebuttal testimony is to respond to specific comments made by
10 other witnesses regarding the implementation and administration of PacifiCorp's
11 2003-A Request for Proposals ("RFP").

12 **Q. What are the specific topics you plan to address in your rebuttal testimony?**

13 A. The specific areas I will address include: (1) the consistency with which the
14 screening criteria were applied to the ranking of offers; (2) clarifying what was
15 intended by the statements regarding the uncertainty surrounding debt imputation,
16 and (3) rebutting claims that Navigant's role as the outside evaluator was less than
17 objective.

18 **II. APPLICATION OF THE SCREENING CRITERIA**

19 **Q. Explain your understanding of the origin of the screening criteria and how
20 the screening criteria were applied.**

21 A. During the process of evaluating the indicative offers submitted by bidders,
22 PacifiCorp relied on the three criteria outlined in the original RFP – economic
23 value, dispatchability, and environmental attributes. Without any foreknowledge

1 of what types of offers bidders would be submitting, PacifiCorp developed these
2 criteria and their respective weightings and made them available to numerous
3 stakeholders during formation of the June 5, 2003 stipulation signed by several
4 intervenors in the current proceeding (“Stipulation”) and as per the RFP reviewed
5 by the Oregon Public Utility Commission. These criteria were then established as
6 the basis for the initial screening of offers in each of the three bid categories. For
7 each offer, the three criteria were taken into consideration in associating a point
8 score for both price and non-price factors. The resulting ranking of offers
9 reflected the score received across each of the three criteria.

10 **Q. Were the screening criteria applied in a manner that was consistent with the**
11 **intent of the RFP?**

12 A. Yes. All three criteria were applied against each one of the offers in the baseload
13 bid category consistent with how it was stated in the RFP and explained to bidders
14 during the Pre-RFP and Post-RFP informational sessions held by PacifiCorp. In
15 addition, the combined criteria were used as the basis to establish the ranking of
16 offers as outlined in the RFP. None of the criteria were excluded. However,
17 given the similarity of offer types in the baseload bid category, the implication
18 was that the screening criteria of dispatchability and environmental attributes
19 alone would not be sufficient to segment the ranking of offers. Once the ranking
20 was established using the three criteria, economic value was the distinguishing
21 variable in the rank order of offers. While the application of the criteria was
22 consistent with the RFP, the similarity of offers based on the dispatch rights and
23 fuel type had the effect of neutralizing these criteria as additional filters.

1 **Q. Did this effect result in any potentially viable offers being unduly excluded**
2 **from consideration in the context of the RFP?**

3 A. No. Notwithstanding this effect, PacifiCorp initiated discussions with each one of
4 the bidders in the baseload bid category who provided an offer that was
5 economically superior to the Company's next best alternative ("NBA").

6 **Q. On page 19, lines 25-27, Mr. Oliver states that the screening criteria were not**
7 **consistent with the original scoring and evaluation process. Do you agree**
8 **with this conclusion?**

9 A. No. The screening criteria were applied in the exact same manner as they were
10 intended in the original RFP. The scoring and evaluation process was
11 implemented using all three screening criteria and reflected the scores received by
12 each bidder, taking into account all of the criteria as it related to each of the
13 offers. Both the price and non-price factor weightings were incorporated into the
14 rankings and resulted in discussions with each of those counterparties. No
15 counterparty that scored high on the price and non-price factor criteria was
16 excluded from the short list.

17 **III. USE OF DEBT INFERENCE IN THE VALUATION OF OFFERS**

18 **Q. Mr. Oliver stated in his testimony, referring to a section of the Navigant**
19 **Final Report, that utilities' treatment of "inferred debt" has some latitude**
20 **given the guidance provided by Standard and Poors ("S&P"). Do you want**
21 **to clarify what was meant in the report by the reference to "latitude"?**

22 A. Yes. Rating agencies typically impute all or a portion of a long-term PPA as debt
23 in their analysis. For instance, S&P starts by calculating an imputed debt

1 component based upon the capacity payments to be paid over the life of the PPA.
2 It does this by taking the net present value of the capacity component of the PPA
3 payments using a 10% discount rate. After it calculates this figure, S&P applies a
4 weighting to this amount based upon the risk level that it sees inherent in the
5 underlying obligation. Take-or-pay contracts typically constitute a 10% to 50%
6 weighting, depending on the cost recovery mechanisms that a utility has in place.
7 Once S&P has a risk-adjusted debt component, that component is added to the
8 capitalization of the utility being rated. S&P then imputes the pre-tax interest
9 payment that would result from the imputed debt component. These imputed
10 numbers become part of the review of the credit. In this process, the latitude the
11 Final Report refers to is the weighting that S&P chooses to attach to a take-or-pay
12 contract between 10% and 50%. Instances of direct debt, as opposed to the
13 inferred debt discussed above, do not afford any flexibility in interpreting whether
14 debt is added directly to the balance sheet.

15 **IV. NAVIGANT'S OBJECTIVITY AS THE OUTSIDE EVALUATOR**

16 **Q. Some witnesses have contended that Navigant was not objective in its review**
17 **and could not have been objective since Navigant did not answer directly to**
18 **the Utah Commission. Do you agree with this assertion?**

19 A. No. As the Outside Evaluator, Navigant's reputation is based on the quality of
20 work that it provides to clients. In cases such as this where Navigant's role, its
21 findings, and its observations of the process become a matter of public record, the
22 need for Navigant to deliver objective, high quality work becomes paramount.
23 From the beginning of the process, Navigant's focus was on ensuring that the

1 process was fair, consistent, and reasonable as per the stipulation. Furthermore,
2 Navigant was required to file both public and confidential reports at various
3 stages of the process documenting its assessment of each stage of the RFP. On
4 top of this, Navigant was available to the Commission and its staff to address any
5 questions it may have had regarding the process and its findings either with or
6 without PacifiCorp being present.

7 **Q. Did the Division’s hiring of another consultant to review (1) the RFP process**
8 **and (2) Navigant’s findings and conclusions provide substantive validation**
9 **that Navigant’s involvement met the intent of the Stipulation?**

10 A. Yes. The Division’s hiring of another consultant to conduct its own independent
11 review after the fact and their finding that the conclusions Navigant came to were
12 supportable provides further validation to the fairness, consistency, and
13 reasonableness of the RFP process as a whole that Navigant found. In light of this
14 additional scrutiny placed on PacifiCorp’s RFP process and Navigant’s reports, I
15 find assertions that Navigant’s involvement was less than objective to be
16 somewhat suspect.

17 **Q. Do you agree with the assertion that Navigant, since it received compensation**
18 **directly from PacifiCorp, could not possibly render an objective opinion**
19 **about the RFP process and acted in an independent manner (UAE, pg 13,**
20 **Lines 8-17)?**

21 A. No. First, Mr. Weir is incorrect in his perception that Navigant “answer[ed] only
22 to PacifiCorp.” While PacifiCorp was responsible for paying Navigant’s bill,
23 Navigant’s responsibility was to report on its findings and observations to the

1 Utah Commission, not PacifiCorp. The error in his assertion is readily apparent
2 in the terminology used in the Stipulation, which states that

3 “the primary role of an independent consultant (Outside Evaluator)
4 should be (1) to make certain that, if PacifiCorp is considering a
5 self-build option or if an affiliate may bid, PacifiCorp does not
6 give any advantage to its affiliate and that it evaluates its own build
7 option in a manner that is reasonable, fair, unbiased and
8 comparable to the extent practicable (“Fair Manner”), against the
9 other bids, and (2) to submit detailed reports [to the Commission]
10 on whether the process followed by the Company adequately
11 meets these objectives”

12 Second, Navigant operated in an independent fashion conducting its own review
13 of the NBA, an independent and separate parallel review of the original RFP
14 responses, and an in depth review of the modeling methodology and results
15 independent of PacifiCorp. All of this was reported in papers that were filed
16 directly with the Commission. Third, the Division inserted another layer of
17 review on the whole process as well as Navigant’s involvement in that process
18 through its hiring of Merrimack Energy, which has testified as to the
19 reasonableness of the process and the resource selection that was made by
20 PacifiCorp (Oliver, pg. 4 lines 1-11).

21 **Q. Does this conclude your testimony?**

22 A. Yes.