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BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application of)
PacifiCorp, by and through its Rocky)
Mountain Power Division, for Approval of)
a Solicitation Process for a Flexible)
Resource for the 2012-2017 Time Period,)
and for Approval of a Significant Energy)
Resource Decision)

**COMMENTS OF LS POWER
ASSOCIATES, L.P.**

Docket No. 07-035-94

LS Power Associates, L.P., through its counsel and pursuant to the Scheduling Order issued by the Public Service Commission on March 4, 2008, hereby submits the following Comments on PacifiCorp's draft Request For Proposals (RFP).

1. LS Power Associates, L.P. is an independent power producer that develops, owns, operates and manages large-scale power generation projects in the United States. LS Power Associates, L.P. and its predecessors and affiliates ("LS Power") have developed eleven individual electric generation facilities in the United States which total approximately 7200 megawatts of generation capacity. LS Power currently has a number of natural gas, coal, and renewable generation projects under development throughout the United States. It has managed for itself or third-party owners over 20,000 megawatts of generation capacity. LS Power has an in-depth and up-to-date understanding of the financial markets as they relate to the financing of

power generation projects. In the past 3 years, LS Power has raised in excess of \$10 billion in debt and equity.

2. LS Power is an active market participant and is interested in supplying Utah with low-cost generation. LS Power participates in many requests for proposals for power generation resources in the U.S. LS Power has reviewed the draft “2008 All Source - Request for Proposals” (the “Draft RFP”) and offers the following comments relating to two primary areas of the Draft RFP: credit requirements and comparability.

Credit Requirements

3. LS Power acknowledges that it is important to establish the creditworthiness and experience of bidders, and to place on bidders the burden to establish sufficient creditworthiness and experience to supply PacifiCorp under a long-term supply arrangement. LS Power’s concern with the Draft RFP is that strict application of unduly high credit requirements will severely limit participation in the process, and limit available alternatives for ratepayers.

4. The need for PacifiCorp to protect itself against the credit of its counterparties is understandable. The approach of requiring bidders to either be investment grade or post security at a certain level is reasonable. Because most independent power suppliers are not investment grade, the industry standard practice is to post security for transactions. However, the required amounts of security in the Draft RFP are unreasonably high, and provide a disadvantage to third party suppliers. Security has a cost associated with it which will increase the cost under a proposal.

5. The levels required in the Credit Matrix place an undue burden on bidders and give PacifiCorp’s self-build options a significant advantage. A reasonable amount of security

should be required in order to balance the need for performance assurance with the costs associated with providing a letter of credit or other security. The requirement of higher levels of credit results in real costs being incurred by the bidders and serves to drive up the price of third party bids. There is a balance between requiring a reasonable amount of credit support to protect the purchaser, and imposing excessive requirements that increase the costs to be incorporated into the proposals and potentially passed on to ratepayers. Ultimately, the level of credit support should be established which does not discourage participation in the process and cause those excessive costs to ratepayers. PacifiCorp's Credit Matrix proposes an unreasonably high level of proposed credit support. While the Credit Matrix presents what appears to be an objective analysis of risk, it is not an approach we have seen in any other RFP in the country and the results are wholly unreasonable.

6. By way of illustration, under PacifiCorp's proposed requirements, the worst case security requirement could be \$120/MWh for every potential megawatt hour delivered over a 5 year term.¹ PacifiCorp contends that this requirement is based on the additional cost of supplying replacement power at some arbitrarily chosen risk-adjusted level. This would imply, based on PacifiCorp's forward price in 2012 of \$91.09/MWh and escalating in years beyond, that replacement power prices would be above \$210/MWh on average for all on-peak summer hours for 5 years. While this example illustrates the "worst case" scenario, even the credit requirements for asset-backed resources are 5-10 times higher than LS Power has negotiated with third-party purchases at arms length for new generation resources.

¹ The Credit Matrix for a non-asset backed resource for a 5-year term beginning in 2016 is \$62,177,400 for 100 MW. For a proposal of Third Quarter power, defined as 16 peak hours from July through September, this results in $\$62,177,400 / (100 \text{ MW} \times 16 \text{ hours per day} \times 5 \text{ days per week} \times 13 \text{ weeks per year} \times 5 \text{ years}) = \$120/\text{MWh}$. Note that this conservatively assumes a 5 x 16 product without dispatch rights. To the extent the resource is dispatchable and has a lower capacity factor, the security requirement may be much higher.

7. The proposed Credit Matrix presents a hurdle that many projects, including those financed on a traditional project finance basis, will not be able to meet. The project finance approach has proven capable of supporting an appropriate and reasonable range of credit requirements that is widely accepted in the industry. LS Power recently financed its \$1 billion Plum Point Energy Station project on a project finance basis, and negotiated security along with the other necessary long-term off-take arrangements with multiple counterparties, to all the parties' mutual satisfaction. LS Power recommends that PacifiCorp adopt a similar approach to avoid imposing unreasonably high costs on the bidders' proposals.

Comparability

8. Several provisions of the RFP present the opportunity for PacifiCorp's own proposals to be evaluated more favorably than third-party bids. The potential lack of comparability troubles LS Power as a potential bidder, and will likely have a chilling effect on some bidders.

9. One primary concern is with the lack of comparability in pricing. Bidders are required to propose a price in which at least 60% is fixed and up to 40% is indexed, although the indexing is limited in scope. It is LS Power's understanding that PacifiCorp's proposal will be an estimate only. As a rate-based proposal, PacifiCorp's bid will be subject to differences in the actual construction costs compared to the estimate, and also subject to differences in the actual financing costs compared to the estimate. In an environment of rising construction costs, and interest rates, its ratepayers are likely to bear the risk that PacifiCorp's bid will not meet the estimate, while third-party bidders are required to assume all interest rate risk and the risk of cost overruns. The result is that bidders are at a significant disadvantage, because their proposals

need to cover the risk of rising construction costs and interest rates. In fact, the same is true for many other factors. Bidders are required (or must be willing), for example, to commit to fuel efficiency operating costs, and unit availability, while PacifiCorp provides only estimates of those items, free from the risk of being aggressively low. The fact that bidders are required to take into account a premium for risk results in a incompatible comparison between the proposals of PacifiCorp's proposals and third-party bidders' proposals.

10. In addition to the disparity between certain requirements for PacifiCorp and those of the bidders, there are significant benefits to third party suppliers such as performance guarantees², increased wholesale competition³, and diversification of suppliers⁴ which are not captured in the evaluation. LS Power recommends that the Commission examine whether the evaluation criteria are designed to yield a fair and reasonable comparison between PacifiCorp and third party bidders.

Conclusion

11. The Draft RFP does not allow for fair and reasonable consideration of third-party bids relative to PacifiCorp's self-build proposals. The credit requirements for third party bids are unreasonably high. In addition, an approach which allows risk-free estimates for a self-build option, and requires fixed price third-party bids lacks comparability. PacifiCorp's bids should be held to the same standards as third party bids, so that the risks and benefits to ratepayers from

² For an extreme example, consider the worst-case scenario of a generation project poorly performs in terms of efficiency and output. In the case of a utility sponsored project, ratepayers will continue to pay the higher fuel costs and the capital cost of the project. In the case of an independent power producer with a power purchase agreement, ratepayers will only pay for fuel at the guaranteed heat rate, and only pay for the actual tested capacity of the facility.

³ Studies have estimated the savings to consumers resulting from wholesale electricity competition in the U.S. at nearly \$5 billion annually.

⁴ Currently, ratepayers have significant exposure to PacifiCorp as the primary supplier of energy. Purchasing power from a third-party supplier under a power purchase agreement diversifies this exposure.

third party bids can be fairly considered in the evaluation. LS Power requests that the Commission consider these comments and take the necessary steps to ensure a reasonable process and a level playing field for all bidders, and to ensure the best outcome for all ratepayers.

Dated this 21st day of March, 2008.

/s/ William J. Evans

William J. Evans

Michael J. Malmquist

Attorney for LS Power Associates

CERTIFICATE OF SERVICE

I hereby certify that on this 21st day of March, 2008, I caused to be e-mailed and/or mailed, first class, postage prepaid, a true and correct copy of the foregoing **COMMENTS OF LS POWER ASSOCIATES, L.P.**, to:

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