



COMPETITIVE PROCUREMENT: A GUIDE TO GETTING THE BEST DEAL FOR CUSTOMERS

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Electric Power Supply Association
*Advocating the **power** of competition*

CNF DISCUSSION AGENDA

- Perspective of Competitive Power Sector
 - Asking the right questions
 - Proper risk management/allocation is essential
 - ‘Reliability Option’ should embrace competitive plants
- CNF Outcome
 - Supply portfolio that best fits customer needs
 - Preserve customer choice and competitive markets
 - Market test for new supply – evaluation equity
 - Comply with intent of current Michigan law

IRP IN THE 21ST CENTURY

- Integrated Resource Planning – 1990
 - Utility-specific; less emphasis on regions
 - Resource planning – traditional supply, renewable sources, customer demand, demand-side management
- Comprehensive Resource Planning – 2005
 - Utility-specific, but regional considerations
 - Role of procurement – a permanent option

Market Competitiveness

- Competitiveness of Markets – Structure/Conduct/Performance
- "Contestability" of Markets – Barriers to Entry
- Competitive Procurement – Improve Contestability of Wholesale Markets
- Procurement
 - Diagnostic role
 - Prescriptive role

BARRIERS TO ENTRY

- Significant Problem
- Manifested in Three Ways
 - Inability to gain access to capital
 - Inability to gain transmission access
 - Inability to gain access to customers
- Three Adverse Effects
 - Prevent economic sales to local utility
 - Prevent economic sales to other customers
 - Reduce likelihood of new market entry

COMPETITIVE PROCUREMENT

- Serves Many Masters
 - Reduces affiliate preference
 - Reduces transmission market power
 - Improves price discovery and market liquidity
 - Improves risk allocation
 - Improves access to capital markets
 - Improves reliability
- Many Approaches to Procurement

GETTING *the*
BEST DEAL
for
Electric Utility Customers

A Concise Guidebook
*for the Design, Implementation
and Monitoring of Competitive
Power Supply Solicitations*



**ELECTRIC UTILITY
RESOURCE PLANNING:
THE ROLE
OF COMPETITIVE
PROCUREMENT AND
DEBT EQUIVALENCY**

Electric Power Supply Association
Prepared by GF Energy LLC

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ESSENTIAL ELEMENTS OF COMPETITIVE SOLICITATIONS

- Importance of Competitive Solicitations
- Holding Credible Solicitations
- Ensuring Proper Solicitation Format
- Fair and Accurate Bid Evaluations



COMPETITIVE SOLICITATIONS

- Recent Focus on Shorter-Term Power Procurement (0-3 years)
 - Load auctions and utility RFPs
 - Emphasis on energy, ancillary service products
- Longer-Term Procurement (3+ years)
 - State-sanctioned solicitations and RFPs
 - Asset-backed capacity and energy
 - Financing vehicle for new infrastructure
 - Price-only auctions to more extensive RFPs

STATE PRUDENCE REVIEWS

- Prudence reviews allow the Commission to review electricity procurements in terms of:
 - Price
 - Risk
 - Reliability
 - Environmental performance
- Competitive solicitations demonstrate prudence by showing that a utility fairly evaluated its full range of both utility and non-utility options.

STATE PRUDENCE REVIEWS (cont.)

- Commission may establish a rebuttable presumption that an approved solicitation results in a prudent investment or procurement decision.
- Such a decision would:
 - Shift burden of proof from utility to intervenors
 - Expedite the regulatory review process
 - Ensure utility cost recovery for contracts signed through the approved competitive solicitation process
 - Obviate need for a “regulatory out” clause in the purchase power agreement

CREDIBLE SOLICITATIONS

- Collaborative Process
 - Local utility submits recommended RFP approach
 - Multi-day, commission-facilitated meetings
 - Commission resolves outstanding issues
- Independent, Third-party Evaluator
 - Performs independent evaluation of the bids
 - Monitors communication between the utility, affiliate
 - Benefit: Extra pair of “eyes”
 - Recent solicitations - ACC, CPUC, GA PSC, PUCO, MD PSC, NJ BPU, UT PSC, WA UTC

CREDIBLE SOLICITATIONS (cont.)

- Fair Process Must:
 - Be free from actual, apparent conflicts of interest
 - Provide all bidders similar access to information
 - Require full public review of the utility decision-making process
- If Utility or Affiliated Entity Participates, Additional Safeguards Required
 - Use of an independent evaluator - reports to commission
 - Separation of utility personnel - utility's proposal vs. evaluating bids
 - Utility winner must honor its bid prices

PROPER SOLICITATION FORMAT

Format and Product Types

- Requests for Proposals
 - Includes price and non-price terms
 - Non-price terms can include capacity sizes, start dates, term lengths, pricing structures
 - Can be harder to compare
 - Manage risks over time
 - Can include demand response
- Price-only Auction
 - Provides greater transparency
 - Limits exposure to regulatory risk





BID EVALUATION PROCESS

Six Key Issues

- Comparability for all bidders
- Transmission assessments of bidders
- Cost-plus offers versus pay-for-performance bids
- Comparing bids with unequal lives
- Creditworthiness concerns
- Balance sheet penalties



DEBT EQUIVALENCE

- Application of Debt Factor to Long-Term PPAs
- Designed to Impute Debt to Utility Balance Sheets
- Originally Applied by S&P in 1990
 - S&P believed utility-owned generation was disadvantaged vis-à-vis PPAs
 - PPA creates risk by triggering an obligation on utilities to pay a minimum amount in the future
 - S&P applies a risk factor to the future value of expected capacity payments in a long-term PPA
 - Resulting dollar amount is added to bids from suppliers in competitive solicitations

DEBT EQUIVALENCE (cont.)

- S&P Views Debt Equivalency from Perspective of Bondholders, not Utility Shareholders, Customers
- State PUCs Can Address Issue from Perspective of Customers and Shareholders
- Issue Just Now Resurfacing at State Level after 12-Year Hiatus from PURPA QF Contracts
- As Competitive Procurement Grows, Debt Equivalency Will Become More Prominent
- Pendulum Has Swung Too Far Against PPAs

DEBT EQUIVALENCE (cont.)

- Two Venues for Treating Debt Equivalence
 - Resource procurement and bid evaluation
 - Utility cost-of-capital proceeding
- COC Appropriate Absent Comparable Bid Review
 - Imposing debt-like risk on PPAs creates an unfair bias
 - PPA cost recovery no more risky than for rate-based generation
 - COC proceedings evaluate utility's financial position on a portfolio basis – the bid evaluation is a “one-off” review
 - COC proceedings are the best arena to balance these considerations, not the competitive bid evaluation

CONCLUSION

- Competitive Plants and Reliability Option: Mutually Reinforcing
- Well-Designed, Managed RFPs
 - Excellent prudence tool
 - Full range of resource options
 - Fits Michigan law
 - Best deal for consumers





Questions

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