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IDAHO PUBLIC
UTILITIES COMMISSION

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Attorney for the Commission Staff

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION OF)	
THE PETITION FILED BY IDAHO POWER)	CASE NO. IPC-E-03-16
COMPANY FOR APPROVAL OF)	AVU-E-03-9
MODIFICATIONS TO THE SECURITY)	PAC-E-03-13
PROVISIONS REQUIRED TO BE INCLUDED)	
IN POWER PURCHASE AGREEMENTS)	
BETWEEN ELECTRIC UTILITIES (IDAHO)	REPLY COMMENTS OF
POWER, AVISTA CORPORATION DBA)	THE COMMISSION STAFF
AVISTA UTILITIES, AND PACIFICORP DBA)	
UTAH POWER & LIGHT COMPANY) AND)	
PURPA QUALIFYING FACILITIES (QFs).)	
)	

COMES NOW the Staff of the Idaho Public Utilities Commission, by and through its Attorney of record, Scott Woodbury, Deputy Attorney General, and in response to the Notice of Scheduling, and in response to Order No. 29515 issued on June 9, 2004, submits the following comments.

BACKGROUND

On November 5, 2003, Idaho Power Company (Idaho Power; Company) filed a Petition with the Idaho Public Utilities Commission (Commission) requesting authority among other things to eliminate the second lien requirement as a risk mitigation measure in PURPA Power Purchase Agreements containing levelized avoided cost rates. Staff objected to the proposed elimination of

the second lien requirement. Staff noted that without a second lien, PURPA Qualifying Facilities (QFs) desiring levelized rates must post 35% liquid funds as security for the calculated overpayment that results from the front-end loading that occurs with a levelized rate structure. Idaho Power in reply comments represented that should the Commission continue with the second lien requirement the Company intended to outsource the legal work and requested that it be permitted to collect the estimated \$1,000 - \$1,500 cost directly from the QF or alternatively recover the lien expense as part of its annual Power Cost Adjustment (PCA) filing. Addressing this issue of cost recovery, Staff contended that this was a contract administration cost and has never been a cost directly billed to QFs; nor was it the type of power cost that was appropriate for recovery through the PCA. Staff opposed the direct billing of this cost to QFs or the recovery of same through the PCA.

On April 27, 2004, the Commission issued final Order No. 29482 in Case Nos. IPC-E-03-16, AVU-E-03-9, and PAC-E-03-13. In its Order the Commission denied Idaho Power's request to eliminate the second lien requirement as a risk mitigation measure for PURPA Power Purchase Agreements containing levelized avoided cost rates. For new levelized contracts the Commission authorized the Company to recover its lien expense from the contracting QFs; or alternatively, permitted a QF to prepare the lien documentation and file the lien itself.

On May 17, 2004, Idaho Power filed a Petition for Reconsideration (IDAPA 31.01.01.331) or in the alternative a Petition for Clarification (IDAPA 31.01.01.325) regarding the portion of Commission Order No. 29482 that provides the option for QFs to prepare and file the lien or security interest documentation. The Company cited the following specific Order language to be of concern:

The Commission continues to find value for ratepayers in the presence of a second lien to secure overpayment liability. We recognize that securing a lien may entail some expense. We assume the Company's decision to outsource is based on a determination that the utility has no in-house expertise or that the cost of outsourcing the task is less than performing the task itself. The Commission finds that it is inappropriate to recover this type of expense as part of the Company's PCA. We find it reasonable, however, for the Company to assess this cost to QFs. Alternatively, we find it reasonable that the QF be permitted to prepare the lien documentation and to file the lien itself. The procedure that we approve for recovery of lien expense is for new levelized PURPA contracts only.

Order No. 29482, p. 12.

The Company also expressed its concern with the following language from the Commission's final Order No. 29482:

For existing levelized PURPA contracts, the Company is expected to administer its contracts in a responsible fashion and to require QF compliance with Commission –292 security requirements. For those levelized QF contracts without a second lien, the QF should be brought into compliance or the Company should require a posting of liquid security. The Commission expects the Company to follow Commission Orders. Reference *Idaho Code* § 61-706. If liquid security is required but not enforced, it is the Company and not its customers that are at risk for the foregone security.

Order No. 29482, p. 12.

On June 9, 2004, the Commission in Order No. 29515 granted reconsideration of that portion of Commission final Order No. 29482 pertaining to the risk mitigation second lien requirements in levelized contracts and the option provided to QFs to prepare and file related security interest documentation. In its Petition for Reconsideration, the Company requested that the QF be required to submit the proposed QF-prepared security interest (second lien) filing to the utility for prior review and approval. The Company also requested that the utility be relieved of any liability, even if it has review and approval authority, should the QF-prepared lien later prove to be insufficient or unenforceable. As part of the reconsideration, the Commission noted that its decision to authorize recovery from QFs of Company legal expenses related to second liens is also at issue.

ANALYSIS

The –292 Second Lien Requirement - Not broken - No need to fix

In its initial Petition in this case recommending elimination of the Second Lien Requirement, Idaho Power represented that QFs were apprising the Company “that the financing structures of existing projects do not allow Idaho Power to place a second lien on the project as required in the –292 case.” IPCO Petition, page 4. The Company considering the QF claims, concluded that “it is possible that the financing arrangements of existing projects would preclude a subsequent lien position by Idaho Power or any other party without the consent of the primary lender.” Petition, page 4.

Further in its initial Petition, the Company states:

In certain cases, the financing arrangements of a CSPP do not allow a second lien position as anticipated in Order No. 21690, as amended. However, where those restrictions do not exist, the Company either places a second lien on a project at the time a levelized rate agreement is executed or at the time a project is amended to conform to the risk mitigation requirements of Order No. 21690, as amended.

The clear inference from the Company's original Petition language is that there existed a number of QFs with levelized rate contracts with no second lien in place. That Staff was of this opinion is evidenced further in Staff's Comments wherein it states "Due to what the Company contends is the marginal value of the secondary lien position *and the inability of the Company, in some circumstances, to obtain security in the form of a second lien*, Idaho Power proposes to delete the secondary lien rights as a risk mitigation measure in levelized rate arrangements with QFs." emphasis added. The Company in reply comments did nothing to disabuse Staff of this misperception. In preparing for reconsideration comments, Staff determined the facts to be otherwise. Staff, in Production Request No. 12, requested that the Company identify all Idaho Power/QF contracts with levelized rates that are subject to the Commission's -292 Second Lien Security Requirement; identify all projects with an existing and filed second lien; and for those QF projects without a second lien indicate whether this was a result of a) administrative neglect by Idaho Power or b) an election by the QF to post liquid security . . .

In response to Staff's Production Request No. 12, the Company identified 25 projects with levelized rates that are subject to the Commission's -292 Second Lien Security Requirements. All of the projects with the exception of one have an existing and filed second lien. The one exception elected to post liquid security in the form of a letter of credit. Staff concludes that the -292 Second Lien Security Requirement was not broken, continued to be of value and required no elimination, adjustment, modification or fix.

Self-Perfection Option

Idaho Power Position

In its Petition for Reconsideration, Idaho Power presented two alternative options: (1) that the Commission eliminate the self-perfection option; or (2) if the self-perfection option is retained, that Idaho Power have the right to review and approve the QF's documentation and

perfection process. Idaho Power addressed both options in its Initial Comments on Reconsideration.

Idaho Power first explains the complexity of the process of perfecting and maintaining a valid second priority security interest for the various types of property comprising a QF project. Due to this complexity of the process and the specialized legal practice it demands, Idaho Power states that it is not comfortable using its in-house legal counsel to prepare and perfect QF second liens. Further, the Company believes that the cost of outsourcing the work is less than the cost of performing the task itself.

Idaho Power also expresses concern with the conflict of interest created by allowing QF developers to prepare and file the documents needed to secure Idaho Power's security interest in the assets of their respective QF projects. *Idaho Code*, Title 28, Chapter 9, the Company notes, sets out very precise documentation and filing requirements to protect security interests. If the requirements are not filed precisely, the security interest is not perfected and is subject to attack in the event of competing creditors seeking to foreclose on the QF's assets. The QF's failure to correctly document, perfect and maintain its security interest in QF project assets would jeopardize the Company's ability to maintain a priority creditor position on the assets covered by the security interest.

Idaho Power maintains that QF developers do not have a proper incentive to do a thorough job of creating and perfecting Idaho Power's security interest. If the Commission still desires to provide this option to QF developers, Idaho Power requests that the Commission clarify Order No. 29482 by requiring that QF developers electing to prepare and file the lien documentation permit the Company to review and approve all aspects of the creation of the security interest. The Company also requests that the Commission clarify that if the QF exercises this option to self-perfect, Idaho Power will have no obligation to take remedial steps if the QF developer fails to adequately cover all project assets or fails to file any required continuation statements to maintain the viability of the security interest over the full-term of the contract.

STAFF RECOMMENDATION

Staff believes that Idaho Power's arguments are compelling for eliminating the QF option to self-perfect second liens. By not allowing the self-perfection option, Idaho Power can avoid incurring additional legal expense that would otherwise be necessary for review and approval of

second liens perfected by the QF. In addition, removing the self-perfection option will alleviate the Company's concern about risk if those security interests are not enforceable or do not cover all of the assets associated with a QF project.

Cost Recovery of Legal Expenses Incurred in Preparing and Perfecting Second Lien

Staff Recommendation

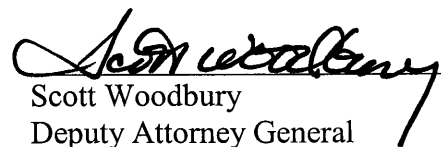
Staff simply reiterates the position it expressed earlier in this case—that the legal expenses of preparing and perfecting a second lien, whether done in-house or outsourced, is a contract administration cost and has never been a cost directly billed to QFs. Staff opposes the direct billing of this cost to QFs. The legal costs attendant to securing a second lien are an operating expense appropriate for consideration in rate case revenue requirement calculations.

STAFF CONCLUSIONS AND RECOMMENDATIONS

Staff concludes that the –292 Second Lien Security Requirement is not broken, continues to be of value and required no elimination, adjustment, modification or fix.

Staff recommends that the Commission rescind its earlier decision to permit QFs to self-prepare and perfect second liens. Staff also recommends that the Commission rescind its decision permitting Idaho Power to recover the cost of legal expenses incurred in preparing and perfecting second liens, directly from QFs, regardless of whether the legal work is performed in-house or outsourced.

Respectfully submitted this 6th day of August 2004.


Scott Woodbury
Deputy Attorney General

Technical Staff: Rick Sterling

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 6TH DAY OF AUGUST 2004, SERVED THE FOREGOING **REPLY COMMENTS OF THE COMMISSION STAFF**, IN CASE NOS. IPC-E-03-16, AVU-E-03-9, PAC-E-03-13, BY MAILING A COPY THEREOF, POSTAGE PREPAID, TO THE FOLLOWING:

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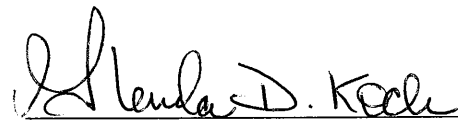
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