

BEFORE THE IDAHO PUBLIC UTILITIES

COMMISSION

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UTILITIES COMMISSION

THOMPSON RIVER CO-GEN, LLC  
a Colorado Company

Complainant

vs.

AVIST CORPORATION, dba Avista Utilities  
a Washington Corporation

Respondent

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Case No. AVU-E-05-07

Testimony of

Lawrence Michael Underwood

on behalf of

Thompson River Co-Gen, LLC

November 9, 2005

1     **Q.     PLEASE STATE YOUR NAME AND BUSINESS ADDRESS FOR THE RECORD.**

2     A.     My name is Lawrence Michael Underwood. My business address is 1610 Wynkoop,  
3     Suite 100, Denver CO 80202

4     **Q.     WHAT IS YOUR POSITION, IF ANY, WITH THOMPSON RIVER-CO-GEN?**

5     A.     I am a partner in Thompson River Co-Gen, LLC (hereafter "TRC"), and am actively  
6     involved in its management.

7     **Q.     WHAT IS YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE?**

8     A.     I graduated from high school in Denver, Colorado, and received a degree in Finance from  
9     the University of Northern Colorado, in 1970. After attending the Naval Aviation Schools  
10    Command in Pensacola Florida, and serving in the U.S. Navy, I returned to Denver in 1975 and  
11    became the finance manager for JHM, Inc. In 1979, I became licensed in the securities business  
12    and spent until 1993 at RAF Financial, with responsibilities in investment banking, corporate  
13    finance, syndicate, and institutional and retail brokerage.

14           From 1993-1995 I was a co-founder and partner of a merchant banking organization.  
15    From 1995 until the present time, I have been involved in assisting companies, both private and  
16    publicly traded, in the areas of corporate structure, finance, and growth. In addition, I have co-  
17    founded and managed companies including Thompson River Co-gen, formed in 2001.

18    **Q.     ARE YOU SPONSORING TESTIMONY?**

19    A.     Yes. I am the policy witness for Thompson River Co-Gen, LLC.  
20

21    **Q.     PLEASE DESCRIBE THE PROCESS BY WHICH TRC DECIDED TO BECOME**

22    **A QF AND SELL POWER TO AVISTA?**

Underwood, Di  
Thompson River Co-Gen, LLC

1     **A.**     The TRC facility, as a topping cycle co-generation facility is by definition a qualifying  
2     facility (QF). The FERC requirement to file a self-certification form is a formality and TRC  
3     decided to wait until it had identified a utility buyer. (See Exhibit No. 2) During the summer of  
4     2004, and after TRC's prior Power Purchase and Sales agreement with NorthWestern  
5     Terminated, TRC looked to identify additional potential buyers of its generation in excess of that  
6     used by Thompson River Lumber Company of Montana. The search was escalated to  
7     neighboring utilities during the period in which NorthWestern was in bankruptcy. We contacted  
8     our attorneys and other consultants in the search for an appropriate buyer, and knew that TRC  
9     met the requirements as a qualified facility, so considered it as a viable option in its search. It  
10    was determined that Avista represented the best fit, given the potential for transmission, the  
11    interconnection, as well as a delivery point in relative close proximity to the plant.

12    **Q.     WHEN DID YOU FIRST APPROACH AVISTA?**

13    **A.**     Mark Thompson, acting as our consultant, contacted Avista concerning the potential sale  
14    of power from TRC, in January 2005, as indicated from the attached letter from Avista, dated  
15    February 4, 2005. (Exhibit No. 3)

16    **Q.     WHAT HAPPENED NEXT?**

17    **A.**     Further conversations took place between Mr. Thompson and Avista through February.  
18    On March 11, 2005, TRC sent a letter to Dave Miller (Wholesale Power Manager, Avista) more  
19    formally introducing TRC, and requested the initiation of contract whereby TRC would sell  
20    energy to Avista under the Avoided Cost Rates for Fueled Projects Smaller than Ten Megawatts.  
21    (Exhibit No. 4)

1 Subsequently, Mr. Miller sent a letter to TRC on March 15, 2005, that acknowledged  
2 TRC's March 11 letter, and requested information about the TRC project, and included a generic  
3 Avista contract for TRC's review. (Exhibit No. 5)

4 Additional discussions took place between Mark Thompson Mike Underwood, and  
5 various Avista personnel concerning the TRC project for several weeks, and on April 26, 2005,  
6 pertinent project information was sent to Avista by Mark Thompson. That information included  
7 a project description, Power Point presentation, TRC-NWE Delivery Agreement, plot plan,  
8 MTDEQ Air Quality Permit, and the Savage O&M agreement. (Exhibit No. 6)

9 On May 3, 2005, a conference call was held with several members of Avista  
10 management, as well as the TRC partners and Mark Thompson. Several different aspects of the  
11 project were discussed including project size, and capability, transmission, and various contract  
12 scenarios. It was agreed to set up a meeting in Boise between TRC and Avista to further the  
13 process in person. That meeting was subsequently scheduled for May 12, 2005 at Avista's office  
14 in Boise.

15 **Q. DID THE MAY 12, 2005 MEETING TRANSPIRE?**

16 **A.** Yes. On May 12, 2005, Benson Lewis, Mark Thompson, and I, met with Bob Lafferty,  
17 Steve Silkworth, Bill Johnson, and a couple of others from Avista. Additional discussion of the  
18 project, power firming by NorthWestern, contracting schedule, roles, the Idaho Public Utilities  
19 Commission, and other topics were discussed. We discussed our desire to develop a contract  
20 under the 10MW Standard Rate published by Avista, and approved by the IPUC. Avista  
21 informed us that we would qualify under the fueled rate structures as opposed to the non-fueled.

1 We also discussed our offer to add a firming capability to ensure firm power delivery through  
2 NorthWestern, at our own expense, as we felt that the IPUC encouraged that firm delivery,  
3 through language included in recently issued orders. We further discussed the ability to sell  
4 NorthWestern any excess energy, in the event we became able to deliver any, and further ensure  
5 that TRC would never exceed delivery of 10 aMW.

6 **Q. WAS THERE ANY FOLLOWUP BY YOU REGARDING THE MAY 12, 2005**  
7 **MEETING?**

8 **A.** Yes. Subsequent to the meeting, telephone discussions between Steve Silkworth and I  
9 took place, where Mr. Silkworth suggested that we consider negotiating a contract under the  
10 Avista IRP Rate schedule. I said that because the plant currently generated less than 10 aMW  
11 our desire was to contract under the 10 MW Standard Rate.

12 I informed Mr. Silkworth that during the testing and evaluation of the plant in the period  
13 after startup, TRC determined that the plant was boiler limited. Our engineers had always  
14 known the plant would be boiler limited because the turbine and boiler were somewhat miss-  
15 matched, although there was no means to accurately measure its ultimate output at that time.  
16 Additional limitations were due to the various equipment that had been purchased and combined,  
17 its new location, new fuels including biomass, and the ambient conditions that had changed from  
18 its prior operating locations. I told him that after startup, we investigated through Elliott and  
19 others, the requirements for increasing the plant capacity to levels that were initially estimated as  
20 possible, and determined that it would mean substantial additional investment. I made it clear to  
21 Mr. Silkworth that given our current investment in the project, before we could justify the

1 additional investment required enabling generation at levels greater than 10 aMW, a contract for  
2 sale above that threshold would have to make economic sense. Mr. Silkworth requested a  
3 schedule of historical generation from the TRC plant, which was delivered to Mr. Silkworth on  
4 May 25, 2005.

5 **Q. WHEN DID YOU NEXT HEAR FROM AVISTA ABOUT THE PROPOSED QF**  
6 **CONTRACT?**

7 **A.** I subsequently had a telephone call with Mr. Silkworth and Bob Lafferty on May 29,  
8 2005 where they discussed concerns over our actual generation exceeding 10MW during some  
9 hours, and that it might be best to try to develop a contract that could accommodate a higher  
10 output. They also requested information on metering points, and an electrical one-line diagram.  
11 I disagreed with their description of the TRC project, as a greater than 10 MW facility, and  
12 reminded them that the plant had never exceeded the @10MW in any month.

13 On June 1, 2005 I sent electrical one-line construction drawings that were developed in  
14 2003 during construction of the plant. A few days later, Dave Miller called to clarify  
15 information on the drawings, and additional information concerning our metering points. We  
16 discussed that the plant output projected in the drawings was obviously based on the engineer's  
17 projected best case scenario, and as we had discussed many times, the plant had not actually  
18 achieved those sustainable levels. I told Dave that the variance between the projected output and  
19 what we actually realized during operations of the plant were one of the reasons we investigated  
20 upgrades to the generation system. I told him once again, that to justify the costs involved in  
21 those upgrades, we would need to demonstrate an economic benefit to the partners in the project.

1           On June 8, 2005 Mark Thompson and I attended a conference call with Dave Miller, Bob  
2   Lafferty and Bill Johnson, where there were further discussions pertaining to TRC's qualification  
3   for the 10MW Standard Rate, and discussion on a contract under the IRP Rate. They also said  
4   that they would not need approval from the Washington Public Service Commission, but needed  
5   to be able to demonstrate that they followed IPUC orders in the development of a contract with  
6   TRC.

7   **Q.    AT ANY POINT DID TRC SUBMIT A CONTRACT PROPOSAL TO AVISTA?**

8   **A.**Yes. On June 14, 2005, Dave Miller requested our review of an electrical one-line  
9   diagram that he had prepared, and with minor modifications we agreed with his diagram. Mark  
10   Thompson included a notation on the diagram showing the projected gross output was boiler  
11   limited, along with a symbol depicting approximate output (~), to reflect that work on the turbine  
12   would be needed to reach the projected generation, with no guarantee of actual performance.

13           Later that day, TRC submitted a letter which addressed Avista's concern regarding  
14   TRC's qualification for the 10MW Standard Rate, along with a proposed contract, executed by  
15   TRC, to Avista for the purchase of 10MW. The letter and contract are attached as Exhibit No. 7.  
16   The form of the contract was one that had been previously approved by the IPUC. TRC took the  
17   initiative to draft the contract, based on our firm belief in the project's qualification, though in  
18   good faith we entertained their suggestion of a negotiated contract. We were frustrated that after  
19   nearly 4 months of dialogue, we were not even near a contract resolution and it was unlikely that  
20   their suggestion of getting close or achieving our terms in a negotiated contract appeared highly  
21   unlikely.

1    **Q.     DID YOU FOLLOW UP WITH AVISTA REGARDING THE PROPOSED**  
2    **CONTRACT?**

3    **A.**     Yes. On June 21, 2005 I had a telephone discussion with Steve Silkworth, and discussed  
4    TRC's desire to move forward with the previously submitted contract. We also discussed TRC's  
5    boiler limited capacity, and I reminded him, as we had done earlier with Dave and others, of our  
6    investigation into investment costs that TRC would incur in increasing capacity. Mr. Silkworth  
7    suggested negotiating a contract under the avoided cost rate structure rather than the Standard  
8    offer rate. Mr. Silkworth again stated that he believed such an approach could satisfy both  
9    Avista's needs as well as our own. Mr. Silkworth further suggested doing so in parallel with  
10   their further investigation into our qualifications for the 10MW Standard offer rate. I said I  
11   would check with the other TRC partners, and get back to him. I also suggested that it might be  
12   prudent to get some direction from the IPUC, as there were clearly differences of opinion on  
13   interpreting the language in prior IPUC orders.

14           The following day, I confirmed with Mr. Silkworth that although TRC firmly believed  
15   that it qualified for the 10MW Standard Rate, that in good faith, TRC would consider negotiating  
16   a contract under the Avista IRP Rate. However, I made it clear to Mr. Silkworth that TRC was  
17   not giving up its right to continue to pursue the 10 MW Standard Rate Contract, as it was not  
18   clear to TRC whether pursuing a negotiated contract would justify the additional investment in  
19   the project to increase the generation capacity beyond the 10 aMW threshold.



1    **Q.     WHAT STEPS, IF ANY, DID YOU TAKE TO FOLLOW UP ON YOUR**  
2    **CONVERSATIONS WITH MR. SILKWORTH REGARDING CONTRACT**  
3    **NEGOTIATIONS?**

4    **A.**     On July 6, 2005 Benson Lewis, Kim Christensen, Mark Thompson, and I had a  
5    conference call with Steve Silkworth, Bob Lafferty, and others from Avista to discuss, in good  
6    faith, the non-binding points of negotiation under the parameters of a negotiated contract which  
7    Avista was proposing. TRC had agreed to consider a negotiated contract if it would not be  
8    economically harmed in pursuing such. The discussion centered on plant operations, and price,  
9    and Avista's attempt to purchase energy at the electric rate stated in their IRP. Mark Thompson  
10   explained that the current market conditions made it impossible for Avista to acquire energy at  
11   their stated IRP electric forecast and such forecast did not truly reflect Avista's avoided cost.  
12   Indeed, Avista has not purchased any long-term resources over the last year at the price stated in  
13   their IRP plan. However, Avista did not agree to negotiate. Therefore acting in good faith in  
14   considering Avista's desire to negotiate a contract, Mark proposed and Avista tentatively agreed  
15   to a hybrid approach in which TRC would sell at an index rate for the first few years and then  
16   begin a contract with Avista. This suggestion, for discussion purposes only, was an attempt to  
17   reconcile the below market rate for the first few years of the contract period, identified in  
18   Avista's IRP plan. It was suggested by Mr. Thompson, and agreed to by Mr. Lafferty, that  
19   perhaps a contract could be developed whereby TRC sold its generation for an initial 4-5 years,  
20   then contract with Avista for the remainder of a 20-year period. This approach would partially  
21   eliminate the disparity between the IRP rate, and the actual near term market prices. Avista also

1 suggested that guidance from the IPUC might be in order, and TRC agreed. The thought of  
2 completing a contract under those terms was eliminated after speaking with the IPUC.

3       Thereafter, on August, 8, 2005 Avista sent their contract under their IRP Rate schedule.  
4 Finally, on August 19, 2005 TRC submitted a Power Purchase Agreement, incorporating the  
5 prior Avista contract, with terms applicable to the 10MW Standard Rate. That contract included  
6 insurance provisions previously included in IPUC prior orders, as well as the language from  
7 prior orders concerning the 10MW generation limitation, and information provided by Mr.  
8 Sterling. (See Exhibit No. 8)

9 **Q. WHAT STEPS, IF ANY DID YOU TAKE TO ANSWER AVISTA'S CONCERNS?**

10 **A.** TRC took every opportunity possible to eliminate Avista's concerns in our eligibility for  
11 qualification under the 10MW Standard Rate. We discussed IPUC prior orders, our boiler  
12 limited generation capability, the other inherent limitations to the plant's generation such as fuel,  
13 and ambient conditions. TRC also provided actual hourly generation data, which clarified that  
14 the Project has never exceeded 10 aMW per month, net of station requirements. Furthermore,  
15 TRC agreed to integrate the Project into Avista's control area (similar to the process Avista  
16 utilized for its other Montana resources, Colstrip and Noxon). This would ensure that the entire  
17 net output was delivered to Avista.

18       We answered every question and request to provide additional information. After  
19 meeting with Rick Sterling, we called Avista and informed them of the discussion and of the  
20 information we learned from Rick. Our consultants and attorneys have extensively examined  
21 prior orders in our desire to ensure that the terms we have included in our contract offering meet

1 the laws of Idaho, and intent of the Commission, and have tried to communicate our objective to  
2 Avista. To the extent possible, we have done everything that we knew to do in order to eliminate  
3 any concerns that Avista presented.

4 **Q. AT SOME POINT, DID AVISTA REFUSE TO NEGOTIATE FURTHER?**

5 **A.** After we submitted our Power Purchase Agreement on August 19, 2005, I was informed  
6 by Dave Miller that Avista would not negotiate the contract further, and suggested that TRC's  
7 best course of action should be to formally address the IPUC.

8 **Q. WHAT WAS AVISTA'S POSITION, IN SO FAR AS YOU KNOW IT?**

9 **A.** We are not entirely clear on the basis for Avista's position, but they have stated that they  
10 do not believe the TRC project is eligible for the standard offer rate, despite the information that  
11 we have provided them. However, Avista has said in the past that because TRC has generated in  
12 excess of 10MW during incremental hourly periods through the startup and testing of the plant,  
13 that we have eliminated our qualification for the 10MW Standard Rate.

14 Further, Avista contends that because the TRC project has been described by its turbine  
15 plated rating and other projected rates through various descriptions of the facility, that the plant  
16 is disqualified from eligibility for the 10MW Standard Rate. They have determined that in their  
17 opinion, the project has the potential to exceed 10 aMW measured monthly, thus it does not  
18 qualify. We have attempted to review previous Commission orders with Avista to no avail.  
19 Thus, we believe, and apparently Avista agrees, that Commission clarification is necessary.

20 **Q. IN PARTICULAR, WHAT WERE THE STICKING POINTS IN THE**  
21 **NEGOTIATIONS?**

1     **A.**     The major sticking point was the qualification for the 10MW Standard Rate. We have  
2     eliminated any other operational concerns by agreeing to integrate the TRC Project into Avista's  
3     control area and deliver the entire, as-available, net output to Avista. TRC included language  
4     that, under normal operating and design conditions, the plant will not exceed 10 aMW monthly  
5     generation, in its contract submitted to Avista. Avista has ignored that TRC has never exceeded  
6     the monthly 10 MW average.

7             Another sticking point was the inclusion of any relationship with NorthWestern that  
8     could result in any potential for financial advantage to NorthWestern, other than the charges for  
9     transmission. To negate any such potential, TRC eliminated any role that NorthWestern would  
10    play except to provide transmission from the plant to Burke, ID, the point of delivery with  
11    Avista. Minor points seem to include insurance requirements included in their draft contract, but  
12    were not consistent with prior approved IPUC orders; TRC simply conformed to those orders.

13    **Q.     DID YOU EVER INFORM AVISTA THAT TRC GENERATED IN EXCESS OF**  
14    **10 AMW IN A MONTH?**

15    **A.**     No. To be perfectly clear, we acknowledged that TRC would need to incur substantial  
16    capital investment to expand the performance of the Project. Only if Avista desired a project  
17    larger than 10 aMW and a negotiated contract resulted that would support the additional  
18    investment would TRC proceed with expanding the Project capability.

19    **Q.     IS IT TO YOUR KNOWLEDGE TRUE THAT TRC HAS NEVER GENERATED**  
20    **MORE THAN 10 AMW IN ANY MONTH SINCE IT WAS BUILT?**

1     **A.**     Yes, TRC has never generated in excess of @10MW, as determined by the actual plant  
2     meter data, which has been provided to Avista, and furthermore, included contract language  
3     assuring that the 10MW monthly average generation will not be exceeded.

4     **Q.     WHY DID YOU CHOOSE TO LITIGATE THIS ISSUE?**

5     **A.**     Because the partners of Thompson River Co-Gen, LLC, firmly believe that the TRC plant  
6     qualifies for the 10MW Standard Rate, issued by Avista, Corp. and approved by the IPUC. We  
7     believe that Avista has taken a position contrary to prior orders issued by the IPUC concerning  
8     the eligibility and other contract points, and that their reasons for refusing to submit our contract  
9     to the IPUC is unfounded, unreasonable, and wrong.

10    **Q.     IS IT TRUE THAT TRC HAD A PRE-EXISTING POWER SALES AGREEMENT**  
11    **WITH NORTHWESTERN?**

12    **A.**     Yes

13    **Q.     TO YOUR KNOWLEDGE, WHAT IS THE STATUS OF THAT AGREEMENT?**

14    **A.**     That contract terminated under its terms in 2004.

15    **Q.     WHAT IS A TEST-POWER AGREEMENT?**

16    **A.**     TRC needed an interim agreement in order to sell power that generated in the course of  
17    startup, tuning, and testing of a plant. The duration of the interim agreement is the sooner of i)  
18    one-year, or ii) TRC's notice.

19    **Q.     IS IT TRUE THAT THE TRC PLANT IS NOW IDLED?**

20    **A.**     Yes. TRC decided to idle the Project while it completed compliance with all air quality  
21    permits.

1    **Q.    WHAT WAS THE REASON FOR IT BEING IDLED, TO YOUR**  
2    **UNDERSTANDING?**

3    **A.**     The Montana Department of Air Quality issued a modified permit to TRC in November  
4    2004, to include changes to the plant completed during construction. That modified permit  
5    actually increased the restrictions on SO2 emissions to a level than was included in the original  
6    2001 permit. The SO2 scrubbing system specified to the 2001 permit could not achieve the  
7    increased levels of reduction required by the 2004 permit, and despite extensive adjustment to  
8    the system from the manufacturer and additional consultants. Therefore, TRC idled the plant in  
9    order to complete the required steps to fully comply with both State and Federal emissions laws.

10   **Q.    WHEN WILL TRC AGAIN BE OPERATIONAL?**

11  
12   **A.**     TRC, its consultants and contractors, are diligently working on completion of the  
13    necessary steps to modify the emissions control systems in the plant in order to meet State and  
14    Federal emissions laws. It is our intent to immediately resume operations upon completion of  
15    those requirements.

16   **Q.    PLEASE DESCRIBE THOMPSON RIVER LUMBER'S ("TRL")**  
17   **RELATIONSHIP WITH TRC?**

18   **A.**     Roger Claridge is the owner of Thompson River Lumber Company of Montana ("TRL").  
19    Roger was an original owner of TRC, owning approximately 30% of the project and a co-signer  
20    on more than \$7.3MM in construction financing. Later, Roger sold his interest to certain of the  
21    other members of TRC, with payments to be made over time. Virtually all of the forty-five year

1 financial and business relationships between TRL and TRC are a reflection of that original  
2 relationship. Roger is the father-in-law of Barry Bates, one of the current TRC members

3 TRL has leased to TRC the approximately ten acre site on which the plant sits, and  
4 provides water to TRC as part of that arrangement. TRC has a 45 year fixed-price contract to  
5 provide steam to TRL for use in its kilns, and to supply the electrical power needs of the mill. In  
6 addition, TRC made capital improvements to TRL's water gathering and distribution system, and  
7 has an arrangement to purchase wood waste from TRL, through a pneumatic delivery system  
8 from the mill to the plant boiler. TRC improved TRL's electrical system. TRC has ongoing  
9 responsibilities for maintaining the water system, electrical system, steam delivery, and wood  
10 waste system.

11 **Q. HAVE ANY LEGAL ISSUES ARISEN DUE TO TRC'S CLOSE RELATIONSHIP**  
12 **WITH TRL?**

13 **A.** The only legal issue pertains to TRL's application for an additional water right to  
14 supplement its ability to supply water to TRC. Avista objected to that application to the Montana  
15 Department of Natural Resources.

16 **Q. DID AVISTA RAISE THIS WATER RIGHTS ISSUE IN ITS DRAFT**  
17 **CONTRACT WITH TRC?**

18 **A.** Yes

19 **Q. WHAT WAS YOUR REACTION TO THAT ISSUE BEING INCLUDED IN THE**  
20 **CONTRACT?**

1     **A.**     It appeared to be an element of leveraging the Avista objection, as an additional  
2     consideration to the contract. I also did not understand it to be relevant in any way to our  
3     contract issues with Avista.

4     **Q.    WHAT STEPS IF ANY WILL YOU TAKE TO ENSURE THAT THE TRC**  
5     **PLANT DOES NOT SELL MORE THAN 10 AMW TO AVISTA IN ANY GIVEN**  
6     **MONTH?**

7     **A.**     TRC has the metering capability to accurately monitor energy delivered to the  
8     transmission system at the plant substation, and to TRL. Although it has never been  
9     demonstrated to have the capability to generate in excess of 10 aMW, TRC has the ability to  
10    reduce or shut down, plant generation to ensure that delivered load will never exceed 10aMW.

11    **Q.    DOES THIS CONCLUDE YOUR TESTIMONY?**

12    **A.**     Yes