BPA Generating Resource Acquisition Process

Bonneville
POWER ADMINISTRATION

August 1990

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BONNEVILLE POWER ADMINISTRATION

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Department of Energy

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SUMMARY

BPA's generating resource acquisition process addresses the need for an efficient procedure to solicit, evaluate, and acquire resources to meet BPA's load obligations. The process also addresses procedural and policy questions related to resource acquisition arising from the 1980 Pacific Northwest Electric Power Planning and Conservation Act (1980 Northwest Power Act, or Act).

BPA coordinated the development of the acquisition process with representatives from the Northwest States and the Northwest Power Planning Council (Council), along with other interested parties. Following an external review beginning in October 1988, the initial draft was revised and circulated for a second round of external review in the fall of 1989. The final process reflects comments solicited in a formal public review conducted in the spring of 1990.

The generation acquisition process pertains to the acquisition of generating resources by competitive means. The Resource Program and Resource Approaches deal with other resource alternatives such as billing credit resources, development of new federal resources, programmatic conservation, and unsolicited resources. The Resource Program also provides guidance for the amount of resources to be solicited for competitive acquisition, the types of resources likely to be offered, and the estimated price at which such resources are expected to be offered.

Competitive acquisition offers BPA the following advantages:

(1) Solicitations can be targeted broadly (for all resources) or narrowly for specific resource objectives

(2) Through the solicitation process, BPA can clearly define its resource needs and match available resources to those needs

(3) Open solicitation may elicit proposals for resources whose availability may have otherwise remained unidentified

(4) Competitive acquisition encourages the systematic evaluation of prospective resources

(5) The structure of the acquisition process can be readily adapted to BPA's authorities and regulatory requirements

In implementing the competitive acquisition system, BPA plans to proceed in the following sequence:

(1) Resource solicitation

(2) Evaluation of proposals

(3) Contract negotiation

(4) Project construction and operational oversight responsibilities

A draft resource solicitation is in development for a competitive acquisition planned for the fall of 1990 and is expected to include, as separate packages, both supply-side and demand-side resources. Results of this competitive acquisition effort will be used to refine BPA's acquisition process.

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I. INTRODUCTION

In October 1988, BPA circulated an initial draft of a process for guiding the acquisition of generating resources. The draft proposed a competitive approach as a starting point for discussions with the four Pacific Northwest States (Oregon, Washington, Idaho, and Montana), the Council, BPA's customers, interest group leaders, and a Technical Review Panel convened for BPA's acquisition process development effort.

These discussions led to the development of the acquisition process described in this document, which is a competitive method through which BPA plans to solicit, evaluate, negotiate, and purchase power from generating resources. The process aims at the efficient acquisition of cost-effective resources with the following objectives:

- Match resources to BPA's resource needs
- Observe statutory requirements
- Manage BPA's risk exposure to acceptable levels
- Ensure that a wide range of resources can be considered
- Address the requirements of other governmental entities vested with resource development responsibilities

The acquisition process is triggered by a determination of resource need that is identified in the Resource Program. BPA arrives at this determination in consultation with the Council. The determination of need will provide guidance concerning the amount of additional resources required by BPA, the portion that may be best met through competitive acquisition, and the types of resources most likely to be favorably considered by BPA.

BPA has developed a separate acquisition process for demand-side resources to address performance differences and separate information and evaluation requirements. Although BPA plans to solicit for both supply-side and demand-side resources at the same time, the proposals will be evaluated separately. BPA plans to combine the economic analysis of supply-side and demand-side resource proposals to yield a single ranking of proposals.

Besides competitive acquisition, other mechanisms available to BPA for meeting load obligations include billing credits, development of new federal resources, additions to existing federal projects, programmatic conservation, and the acquisition of unsolicited resources offered to BPA. These mechanisms were identified and discussed separately in Resource Approaches, a supplement to the 1990 Resource Program.

II. THE RESOURCE PROGRAM

A. The Resource Program and Determination of Resource Need

BPA relies on its Resource Program and the Council's Northwest Conservation and Electric Power Plan (Plan) to determine new firm power needs. The Resource Program estimates the need for additional power to meet BPA's firm loads, taking into account the projected growth in BPA's firm load obligations and estimates of future resource availability and cost. BPA's ability to market surplus power is also considered in determining the need for new resource additions.

Additional information provided by the Resource Program includes estimates of the availability of new resources (in MW) and the expected costs of those resources. These estimates are based on supply forecasts that represent estimates of various resources (hydro, geothermal, residential and commercial conservation, etc.) available to BPA over time at different costs.

B. The Resource Program and Competitive Acquisition

BPA plans to use a mix of approaches to meet new firm power needs. BPA will meet some portion of the need for additional firm power through competitive acquisition. Besides competitive acquisition, efficiency improvements in the hydro and transmission systems, capacity/energy exchanges, and imports from outside the region are acquisition approaches that are also available to BPA.

BPA plans to select proposals for new generating resources and firm power offers based on the amount of new firm power needs indicated in the solicitation. In doing so, BPA will use the information provided by the Resource Program (e.g., quantities of new resources that may be available at various prices) as guidance. For example, if a Resource Program estimates that 200 MW of firm power can be cost-effectively met with new hydro, then new hydro would be selected, but only if it was among those offers which most cost-effectively met the need for new firm power.

If BPA receives resource proposals and firm power offers that exceed the acquisition target indicated in the solicitation, BPA will first select the lowest cost set of resources that is consistent with the acquisition target. BPA will then decide whether to select additional new resources or firm power offers which fall below the overall system cost target.

If an insufficient amount of new resources or firm power offers that fall below BPA's system cost target are submitted, BPA will decide whether to raise the cost target. This determination will be conducted by comparing these higher-than-expected-cost new resources and firm power offers to the alternative acquisition approaches mentioned above. If the least-cost approach to meeting the need for new firm power is to acquire the higher-cost new resources and firm power offers, then the cost ceiling will be raised. BPA may instead determine that the least-cost approach to meeting the need for new firm power is to rely on the alternative acquisition approaches available to BPA.

Because the goal of the acquisition process is cost-effective resource acquisition, the process is not intended nor designed to aid the development of certain technologies or subsidize particular types of resources.

1. Cost-Effectiveness

Section 3(4) of the 1980 Northwest Power Act stipulates that BPA resource acquisitions must be cost-effective. A resource is cost-effective if it meets or reduces BPA's load obligations at a cost no greater than the least costly resource with similar reliability and availability. The determination of cost-effectiveness is based on resource costs, where such costs include all direct costs attributable to the resource, including direct environmental costs.

BPA plans to rely in large part on resource system costs in evaluating resource offers; however, current resource evaluation methods and data limit what resource development impacts can be reflected in system cost estimates. (Many of the resource characteristics that may be reflected in a resource's cost are discussed in a later section). The process for reflecting such factors in system cost is expected to require modification of the sponsor's offer price for cost-effectiveness determination. Such modifications will be performed to rank resources and will not affect the actual schedule of offer prices.

Other resource evaluation factors are likely to be qualitative. The state of evaluation does not allow for the full range of factors affecting resource reliability and availability to be reflected in system cost. BPA plans to specify any and all such non-price factors in each resource solicitation.

2. Resource Ranking

BPA plans to prioritize resource proposals that complete the evaluation process, taking into consideration system cost and non-price factors. In this way, each resource's system cost, non-quantifiable environmental impacts, and non-quantifiable factors affecting resource availability and reliability, will be reflected in the negotiation priority.

C. Unsolicited Resource Proposals

BPA defines an unsolicited resource proposal as one that is received outside the formal resource solicitation period. To provide the broadest scope to its resource acquisition efforts, BPA plans to continue accepting resource proposals submitted outside the formal solicitation period. However, there are special considerations affecting the acceptance and evaluation of unsolicited resource proposals.

BPA has structured its resource acquisition process to take advantage of administrative economies available in the competitive acquisition approach. In the competitive acquisition period, BPA plans to organize its analytic, programmatic, financial, and administrative staff resources to achieve the best work efficiency. Resource proposals submitted in response to a formal solicitation are thus likely to receive more thorough review than otherwise, when staff workload demands may force BPA to delay the evaluation of

unsolicited resource proposals or return the proposals for resubmission during the next formal solicitation period. The opportunity for more prompt and thorough review of resource proposals is therefore greater if the proposal is submitted as part of the formal solicitation.

To ensure impartiality, unsolicited proposals will be subject to the same evaluation criteria, cost-effectiveness testing, and environmental compliance and system compatibility reviews that are applied to proposals received as part of the formal solicitation.

III. COMPETITIVE ACQUISITION

BPA's approach to competitive acquisition incorporates elements from competitive bidding systems currently being used by regulated utilities. However, BPA's approach recognizes substantial differences between BPA and these utilities, and is tailored to meet BPA's needs.

BPA's competitive approach offers several flexibilities in the resource acquisition process:

(1) Resource solicitations can be targeted broadly (for all resources) or more narrowly for specific resource objectives

(2) Through the solicitation process, BPA can clearly define its resource needs and match available resources with those needs

(3) Open solicitation may elicit proposals for resources whose availability may have otherwise remained unidentified

(4) Competitive acquisition encourages the systematic evaluation of prospective resources

(5) The structure of the acquisition process can be readily adapted to BPA's authorities and regulatory requirements

In implementing the competitive acquisition system, BPA plans to proceed in the following sequence:

(1) Resource solicitation

(2) Proposal evaluation

(3) Contract negotiation and execution

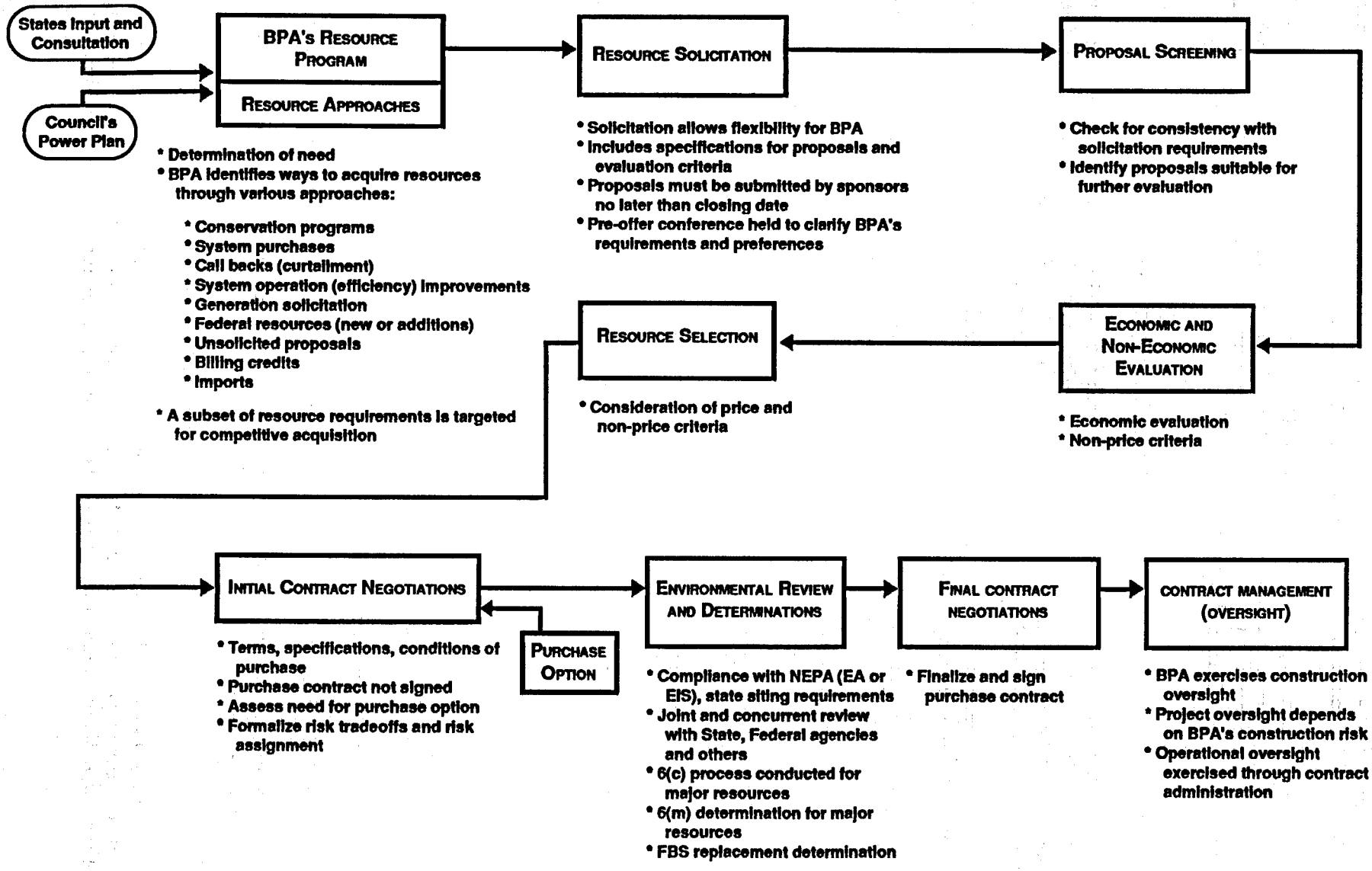
(4) Project construction and operational oversight responsibilities

Figure 1 describes the relationship of the acquisition steps to the Resource Program.

A. Resource Solicitation

In general, BPA plans to conduct resource solicitations that are unrestricted in terms of eligible generating resource size or technologies to provide a wide range of choices for meeting resource needs. However, the

Figure 1
Flow Diagram
BPA Generating Resource Acquisition Process



statement of resource need developed in each biennial Resource Program, along with the identification of desirable resource characteristics for each solicitation, may influence the types and sizes of resource technologies that are offered to BPA. Targeted solicitations, which focus on specific categories of resources, may be used to meet specific resource objectives.

Through its published solicitation, BPA plans to provide sponsors with information on BPA's resource needs and system operating characteristics that will aid in the development of competitive resource proposals. BPA will, in turn, require specific information about each prospective project in order to evaluate proposals in a consistent manner.

In its solicitation, BPA plans to include a set of power purchase contract principles that BPA expects to negotiate with eligible sponsors. BPA also plans to conduct a pre-offer conference to clarify the solicitation to interested parties.

B. Overview of Proposal Evaluation

In order to tailor the evaluation approach to each solicitation, BPA plans to include the evaluation approach as part of the solicitation package. BPA will employ a multi-stage evaluation process designed to identify the most promising proposals for further analysis. Each subsequent analysis will be more rigorous than the previous stage. BPA will structure the evaluation stages to address the following issues:

(1) Sponsor responsiveness and compliance with any threshold criteria

(2) System cost of the proposal

(3) Resource viability

(4) System integration and stability impacts

(6) Non-price environmental impacts

Since Bonneville plans to solicit firm energy, the economic evaluation will be designed to determine the system cost of providing firm energy. To determine system cost, Bonneville plans to consider the following adjustments to a sponsor's offer price:

(1) Resource location

(2) Quantity of capacity provided by the resource

(3) Contract length

(4) On-line date

(5) Displaceability

(6) Seasonal distribution of firm energy

(7) Interconnection costs borne by BPA

(8) Environmental impacts

Including capacity in the determination of each proposed resource's system cost assures that the value of capacity additions are accounted for.

Resource availability, reliability, and environmental impacts are evaluation factors referenced in the 1980 Northwest Power Act's definition of cost-effectiveness. Whether a resource will be available when needed (availability) and whether it will operate as expected (reliability) are also resource development and operating risks. These risks shall be included as part of estimating resource cost when BPA is able to establish cost impacts for different degrees of availability and reliability. In cases where no estimation is possible, availability and reliability shall be included as part of the qualitative assessment of the resource. This will hold true for environmental impacts directly attributable to the resource.

The assessment of resource viability will be designed to evaluate proposals for availability and reliability. BPA plans to assess resource viability based on the following factors:

(1) Development team experience

(2) Financing plan

(3) Project design

(4) Transmission and distribution system availability

(5) Fuel supply security and thermal host

(6) Permits and licenses

(7) Site control

Operations and evironmental impacts which cannot be included in system cost will be included in evaluations when appropriate.

C. Purchase Contract Negotiations

1. Negotiations

BPA plans to enter into negotiations with sponsors immediately after compiling its short list of eligible proposals. The starting point for negotiations will be the contract principles which BPA plans to include as part of the solicitation package. Although BPA plans to negotiate with eligible sponsors for projects whose MW total corresponds with the acquisition target indicated in the solicitation, BPA may elect to negotiate for a MW total that is less than or in excess of the published target.

2. Resource Optioning

BPA will consider using both long-term and short-term option contracts in acquiring resources. Option contracts may take the form of "resource-banking" options, which are intended to reserve construction of sited and/or licensed projects until there is a greater certainty of need, or "purchase options," which are intended to preserve BPA's right to purchase resources until BPA's NEPA responsibilities are fulfilled.

a. Resource-Banking Options (Long-Term)

The Council introduced the concept of long-term resource optioning in its 1983 Plan to address the problem of load/resource uncertainty. The Council's approach involved the following procedure: (a) identify potentially desirable resources, (b) secure a long-term option on these resources, (c) complete the preconstruction phase of project development (including licensing and permitting), and (d) complete the construction of the project on an as-needed basis. In the Council's view, resource-banking regulates resource investment expenditures according to the level of load/resource uncertainty within the planning horizon, since the greatest commitment of resource development expenditure (at the construction stage) is decided when load/resource uncertainty is lowest.

As a test of resource-banking, BPA acquired options on two small hydroelectric project sites in Idaho. The purpose of the test was to identify federal, State, and local statutory, regulatory, and procedural impediments to resource-banking. Preliminary results indicate that the resource-banking concept needs substantial refinement before it can provide a reliable and effective means of managing resource planning uncertainty. BPA is evaluating resource-banking based on this experience and is working with the Council to improve the effectiveness of resource-banking. BPA has proposed the optioning of sites for two combustion turbines (840 MW total) as part of its resource contingency planning.

b. Purchase Options (Short-Term)

The acquisition of a resource is a federal action with the potential for major environmental impacts. BPA is required by the National Environmental Policy Act (NEPA) to conduct a comprehensive environmental impact assessment of any proposed resource acquisition before signing a purchase contract. BPA's environmental review staff estimates that a full NEPA review could take two years or more to complete. This timeframe may affect BPA's ability to secure attractive resources within a competitive resource market.

During the NEPA review period, BPA plans to secure selected eligible resources with purchase option contracts, in which sellers will give BPA an irrevocable option to purchase the resource in exchange for monetary and/or other compensation. The compensation should reflect both the seller's valuation of market opportunity-cost for the project during the option period, and BPA's valuation of the resource. Provisions in the option agreement will allow BPA to terminate the option contract if the project is disqualified during NEPA review.

D. Environmental Review and Other Determinations

1. Environmental Considerations

Because BPA's resource acquisition decisions take into account potential environmental impacts, environmental factors will influence BPA's resource selection. These environmental factors will be addressed in the resource evaluation process and through BPA's NEPA review. All environmental analyses and reviews will be completed prior to contract signing.

a. NEPA Review

As mentioned elsewhere in this document, NEPA requires BPA to conduct an environmental review of any proposed project to determine possible environmental consequences. BPA must complete this review before signing a purchase contract for the project. This procedure could take two years or more to complete, depending on the complexity of the environmental impact analyses required. Because NEPA provisions are applicable to all federal agencies, the involvement of a federal agency in the development of a resource exposes the purchaser of that resource to the impact of the timeframe for completing NEPA review.

BPA plans to expedite fulfillment of its NEPA responsibilities by conducting portions of the overall environmental impact evaluation, where permissible, in advance of specific project reviews. To accomplish this, BPA plans to prepare a programmatic environmental impact statement (EIS) on the Resource Program. In addressing the generic environmental impacts of specific resource types, the Resource Program EIS is intended to expedite BPA's environmental review responsibilities during the solicitation period by limiting the scope of review for individual resource proposals to site-specific environmental reviews. In addition, BPA expects to minimize any duplication in the environmental review of individual projects by working jointly, to the maximum extent possible, with State and federal agencies in their environmental review processes.

b. Protected Areas

As part of the implementation of the Act's fish and wildlife mitigation and enhancement mandate, the Council designated specific areas around the Pacific Northwest as protected from encroachment for power development and incorporated these designations into its current Power Plan. Accordingly, a resource proposed for siting in a Council-designated protected area is not likely to be considered as favorably by BPA as one which is not located in a protected area. A list of fish and wildlife protected areas is available from the Council.

2. Determinations

Before BPA can execute a purchase commitment for a resource, certain determinations must be made. As mentioned elsewhere, all resource acquisition decisions are subject to environmental review by BPA. For major resources (50 aMW or more for five years or more), BPA must also meet the 1980 Northwest Power Act's Sections 6(c) and 6(m) requirements. BPA is developing a statement regarding the determination of Federal Base System (FBS) replacement status for resources to be acquired through competitive acquisition. BPA plans to discuss this issue with interested parties prior to the resource proposal submittal date in the next solicitation period.

a. Section 6(c)--Determination of Consistency With Council Plan

Section 6(c) of the 1980 Northwest Power Act requires that BPA institute a public notification process in the acquisition of a major resource. The process is outlined in the Act and requires that the Administrator determine whether a proposed acquisition of a major resource "is either consistent or inconsistent with the Plan or, notwithstanding its inconsistency with the Plan, [to issue] a finding that [the proposed resource] is needed to meet the Administrator's load obligations under the Act." (Sec. 6(c)(1)(D)(i))

In meeting its Section 6(c) obligations, BPA will rely on its Section 6(c) policy, adopted November 1986. The first step in the 6(c) process is the publication of a notice of the proposed acquisition in the Federal Register, and the transmittal of a copy to the Council, the governor of each State in which facilities would be constructed, and BPA's customers. The publication of the notice is followed by one or more formal public hearings, the development of a written record of the hearings, and the Administrator's official determination of consistency with the current Power Plan.

A copy of the determination will be provided to the Council and disseminated for public notification. Following the receipt of the notice, the Council is required to determine the consistency of the proposed acquisition with its current Plan. In the event that the Administrator or the Council finds that the proposed acquisition is not consistent with the current Plan, the Act provides for additional steps before acquisition, including Congressional action.

b. Section 6(m)--Utility Participation in BPA Acquisitions

Section 6(m) of the Northwest Power Act requires that the Administrator "... determine in each case of a major resource acquisition that a reasonable share of the particular resource, or a reasonable equivalent, has been offered to each Pacific Northwest electric utility for ownership participation or other sponsorship, but not in excess of the amounts needed to meet such utility's Regional load." The process for accomplishing this is not outlined in the Act.

BPA has not acquired a major resource since passage of the Act and has not yet developed a formal process for implementing Section 6(m). BPA plans to develop a process for implementing Section 6(m) prior to acquiring new resources.

c. Section 9(h)(1)--PUHCA Exemption Provision

The Public Utility Holding Company Act (PUHCA) exposes the subsidiaries of electric utilities, when owning the facilities for and engaged in the generation of electric power, to regulation under a variety of provisions. Section 9(h)(1) of the Act provides an exemption from certain PUHCA obligations for such entities when selling power to BPA. In order to qualify for the exemption, the sale must meet certain conditions outlined in the Act, including but not limited to: (1) at least 90 percent of the electricity generated by the entity must be sold to BPA; (2) the organization of the

entity must meet certain PUHCA requirements; and (3) the sale to BPA must comply with the Act's Section 6(m) provisions concerning the offer of participation to Pacific Northwest utilities.

E. Contract Management and Project Oversight

Section 6(i) of the Act describes BPA's oversight responsibilities for resource acquisitions, major resources for which billing credits are granted, and conservation activities. Resource acquisition and billing credit contracts must contain terms and conditions as will:

(1) insure timely construction, scheduling, completion, and operation of resources, (6(i)(1))

(2) insure that the costs of any acquisition are as low as reasonably possible, consistent with sound engineering, operating, and safety practices, and the protection, mitigation, and enhancement of fish and wildlife, including related spawning grounds and habitat affected by development of such resources (6(i)(2))

(3) insure that the Administrator exercises effective oversight, inspection, audit, and review of all aspects of such construction and operation (6(i)(3))

The Act also requires that:

(4) Such contracts shall contain provisions assuring that the Administrator has the authority to approve all costs of, and proposals for, BPA approval for major modifications in project construction, scheduling or operations, including major contract awards or modifications, and to assure that the Administrator is provided with such current information as he deems necessary to evaluate such construction and operation. (6(i)(4))

Since BPA expects that its oversight activities will directly reflect its share of project risk, the nature and extent of BPA oversight for each project will be described in the purchase agreement. The assessment of project risk will be incorporated in the resource evaluation process, including the assessment of both price and non-price factors. The placement of various project risks among BPA and the sponsor, and the costs associated with the assumption of such risks, are part of the determination of both cost-effectiveness and project desirability.

F. Interconnection/Integration of Resources

One of BPA's primary responsibilities is the safe, reliable, and efficient operation and maintenance of the Federal Columbia River Transmission System. BPA therefore participates in the interconnection/integration of all resources with the Federal transmission system, regardless of whether the resources are acquired by BPA or another utility.

BPA has adopted trial standards for the interconnection of small generating resources (50 peak MW or less) in order to assure system reliability, the safety of BPA employees and others, and the efficient

delivery of power. These standards are also applicable to resources above 50 MW. Any resource to be interconnected/integrated with the BPA system shall be in compliance, as applicable, with the trial standards, the Western Systems Coordinating Council and Northwest Power Pool minimum operating reliability criteria, the BPA reliability criteria, the National Electrical Code (ANSI C1), National Electrical Safety Code (ANSI C2), State and local electrical codes, and the general contract provisions of the agreement between BPA and the generating resource or interconnected utility.

IV. WORKING WITH OTHER GOVERNMENTAL ENTITIES

The demands of siting, permitting, and environmental review of prospective resources require that BPA coordinate its acquisition efforts with various federal, State, and local governmental entities. With the large number of agencies vested with resource development responsibilities, BPA recognizes the need for close coordination throughout the acquisition process. BPA plans to continue working closely with other governmental entities in the siting and development of generating resources, in accordance with Section 10(a) of the Northwest Power Act, which directs that "... nothing shall be construed to affect or modify any right of any State or political subdivision thereof or electric utility to ... make energy facility siting decisions, including, but not limited to, determining the need for a particular facility, evaluating alternative sites, and considering alternative methods of meeting the determined need."

At BPA's request, each of the four Pacific Northwest States documented their resource siting and permitting processes (including the requirements of involved federal agencies). BPA then conducted extensive discussions with the States on jointly meeting all parties' environmental responsibilities. While BPA must make its own NEPA determinations, BPA seeks to avoid any added burden on project sponsors by coordinating review processes with other governmental entitities to the maximum extent possible. In addition, BPA plans to integrate the NEPA and 6(c) processes, where feasible, for administrative efficiency.

BPA expects that federal land management agencies such as the U.S. Forest Service, U.S. Bureau of Land Management, and U.S. Environmental Protection Agency, along with other federal agencies vested with statutory and/or regulatory responsibilities affecting power development, will participate in joint review efforts with BPA. BPA acknowledges that State agencies are receptive to joint review efforts, where feasible, to better coordinate the federal NEPA and State environmental reviews.

V. BPA POWER SALES CONTRACTS ISSUES

Section 5 of BPA's utility power sales contract (PSC) requires each customer utility to use its best efforts to either serve its own load growth using firm resources, or to make available to BPA, resources that are equivalent to the customer's load growth under the PSC. This obligation affects the customer utility's right to any excess intra-class power entitlements if BPA's resources are insufficient to serve all of BPA's firm obligations.

A customer utility's submission of an unsuccessful resource offer will not be considered by BPA as contributing to or wholly constituting a "best effort" in meeting this PSC Section 5 obligation. Further, BPA will not consider a utility's willingness to provide wheeling services for any resource acquired by BPA as contributing to or wholly constituting a "best effort" in meeting this PSC Section 5 obligation.

VI. WORKING WITH THE PUBLIC

BPA views regional public acceptance of its resource decisions as a crucial part of the resource planning and development process. BPA expresses its commitment to public participation in resource management through the Resource Program, Resource Approaches, Programs in Perspective, and other resource planning/public involvement programs where interested parties are given an opportunity to review BPA's resource planning proposals and comment on staff recommendations, methodologies, and findings.

BPA's section 6(c) policy provides for public participation in the acquisition of major resources. However, the Act does not require a similar process for the acquisition of non-major resources. Opportunities for public comment on non-major resources are provided instead during the project siting and licensing hearings, which are conducted by the U.S. Federal Energy Regulatory Commission (FERC) and various State and local agencies.

BPA is also developing a mechanism for informing interested parties on the progress of its resource acquisition efforts. However, BPA plans to respect sponsor confidentiality requirements associated with the competitive nature of its acquisition process, avoiding open disclosure of project proposal details in the conduct of the evaluation process. Open disclosure could discourage submission of resource proposals and limit access to the full range of resources available for development within the region.

While BPA does not plan to offer direct public participation in its resource evaluation, assessment, and selection procedures, BPA encourages public comment in the Resource Program and other resource planning and management activities that bear on BPA's resource acquisition decisions.

APPENDIX A

THE CONTEXT OF BPA'S ACQUISITION PROCESS DEVELOPMENT

BPA's resource acquisition process has been influenced by two central features of the regional electric utility environment--competitive bidding within the regulated utility sector and the Northwest Power Act's resource acquisition mandates.

A. Competitive Bidding and BPA's Resource Acquisition Process

Competitive bidding initiatives around the country have developed almost exclusively within the regulated utility sector, in response to factors associated with recent regulatory changes that affect investor-owned utilities (IOUs). These factors include: (1) the administrative determination of PURPA-related avoided costs, (2) uncertainty of cost recovery for resource investments, (3) recent FERC Notices of Proposed Rulemaking (NOPRs) dealing with competitive bidding, independent power producers (IPPs), and avoided cost determination, (4) least-cost planning requirements established by local utility regulatory bodies, and (5) the formation of unregulated utility subsidiaries for power development. These factors work together in shaping the form of competitive bidding that is commonly practiced by regulated utilities.

1. PURPA Avoided Cost Determination and the FERC NOPRs

Recent FERC NOPRs (which do not apply to BPA) advance competitive bidding as an alternative to the administratively determined full avoided cost (ADFAC) methodology used by most utility regulatory bodies for setting PURPA-related avoided cost levels. This approach relies on a market determination of alternative resource prices and establishes full avoided cost levels that may be based upon, or influenced by, power acquisitions from independent, non-utility resource developers. In turning to the independent resource market, competitive bidding seeks to exploit competitive market dynamics in securing lower avoided cost levels than would be obtained through ADFAC methodology.

2. Uncertainty of Cost Recovery for Resource Investments

The "regulatory compact" between utilities and regulators, which provided virtual assurance of cost recovery for resource investments in exchange for generally lower rates of return, was disrupted following the period of intense thermal resource development beginning in the early 1970s. As IOU resource investments encountered unanticipated adversity, utility commissions began applying "used and useful" criteria in prudence reviews for denying part or all of utilities' cost recovery claims. In response to this disruption of the compact, many utilities now follow risk management strategies that aim at shifting resource development risks onto independent resource developers or onto unregulated subsidiaries which can earn investment returns commensurate with risk. Many utility commissions have developed formal competitive bidding programs that enable regulators to oversee the entire acquisition process, thereby implicitly providing increased assurance to utilities of cost recovery during ratemaking.

3. Least-cost Planning

Some public utility commissions have required utilities to submit least-cost resource plans outlining acquisition strategies and goals that are intended to protect ratepayers from unnecessarily expensive new resource facilities. Competitive bidding provides a mechanism for implementing these least-cost plans that rely on competition between prospective resource providers for capturing the greatest economies in the new resources market. Where utilities conduct resource acquisitions outside the competitive process, least-cost plans provide a yardstick for assessing the economies of these new resources within the context of an individual utility's operations, and thereby provide regulators with a baseline for prudence review of these resources during the ratemaking stage.

4. Formation of Unregulated Subsidiaries

Many competitive bidding programs permit "self-dealing," where unregulated generating and power marketing subsidiaries are allowed (under varying levels of scrutiny) to compete on resource solicitations issued by their parent or affiliated utility companies. This enables utilities to detach the higher-risk generation component from the lower-risk bulk transmission and retail distribution parts of the company, while retaining combined revenues within a single corporate entity.

Competitive bidding also provides more efficient access to independent resource developers, who are increasingly being perceived within the utility industry as potentially more efficient resource providers than traditional vertically-integrated utilities. Unregulated subsidiaries provide utilities with investment mechanisms for redeploying capital accumulated through purchasing output from independent resource developers, in ventures that may realize a higher rate of return than otherwise available through their regulated parent or affiliated utility company.

5. Implications For BPA

BPA has closely followed the development of competitive bidding for two reasons: first, because of the potential economies resulting from the competitive resource market, and second, because of the potential for systematic consideration of a wide range of resources, some of which might not otherwise be made available to BPA. Since BPA is not able to own resources or develop them directly, a method which assists BPA in identifying cost-effective resources has significant value. In addition, a competitive approach offers value by introducing market information into BPA's planning system, may be less staff intensive than centrally-designed programmatic approaches, and has the potential to attract resources which may not otherwise be made available to BPA.

Unlike regulated utilities, BPA would not use a competitive approach to meet PURPA obligations, as an alternative to administratively determined avoided cost, or as an alternative to its own construction. While BPA can learn much from observing other utilities as they undertake competitive processes, BPA cannot adopt the competitive bidding approach without tailoring it to its own needs.

B. 1980 Northwest Power Act

The Northwest Power Act establishes a set of constraints and requirements that BPA addresses in its resource acquisition process:

1. The Council Plan

In its 1986 Power Plan, the Council requested that BPA develop a resource acquisition process. The Council observed that loads could grow more rapidly than anticipated, and that BPA might benefit by securing a site-banking option on a major generating resource or capture economies associated with "lost-opportunity" resources by acquiring extremely low-cost, currently available resources ahead of the actual need for the output from these resources. In addition, the Council indicated that certain resource acquisitions may prove desirable in order to test elements of BPA's final resource acquisition process, or to demonstrate new resource technologies.

2. Council Planning and BPA Solicitation

BPA intends to continue to work closely with the Council on development of the Council's Plan, with a goal of reaching agreement with the Council on the types, amounts, and costs of new resources that BPA acquires. BPA expects this agreement to be reflected in the Resource Program, which guides the development of BPA's acquisition targets. Agreement with the Council will be reflected in the resource evaluation criteria and economic evaluation process employed by BPA. In these ways, BPA's close work with the Council will help assure that BPA's competitive resource acquisitions are consistent with the guidance provided by the Council's plan. BPA expects that this will apply to both major resources, which require a 6(c) determination, and non-major resources.

APPENDIX B

OVERSIGHT PRINCIPLES FOR HIGH-RISK PROJECTS

1. General Principles

For the purposes of managing its project oversight activities, BPA views risk in a way that is similar to cost-reimbursability in the contract management process. The greatest level of risk is associated with full-cost reimbursability, which requires substantial government authorities. In such a relationship, BPA views its role vis-a-vis the project owner/operator as contracting agency and contractor, and plans to manage such a contract with the goal of ensuring best value for its investment through safe and economical project construction and operation.

While it is not BPA's intent to engage in day-to-day project management activities, BPA requires full information, received on a timely basis, to protect and exercise its project responsibilities. Further, BPA will reserve appropriate contractual rights to maintain control of costs. Such requirements include timely access to adequate information in order to develop and affect policy, develop plans and provide recommendations on major issues, execute routine administrative and contractual activities related to construction and operation of acquired generating resources, provide guidance and control to assure that program objectives are achieved within established budgetary constraints, and provide for the effective exchange of organizational perspectives between BPA and the project owner/operator. To accomplish these goals, BPA requires active involvement at an early stage in the decisionmaking process.

In exercising its contract management role, BPA plans to:

(1) Maintain a presence at each generating project to demonstrate BPA's resolve in fully protecting its interest and receiving its complete contractual entitlements

(2) Keep continuously informed of the status of each project (with reference to specific contractual provisions) in order to ascertain (a) the extent to which BPA is currently receiving, and (b) the likelihood of continuing to receive, its contractual entitlements

(3) Exercise BPA's contractual rights to direct any action taken by project owner/operators to adjust output, construction or maintenance schedules, and approve or disapprove specific changes to project design, budget, or scheduling

(4) Influence actions proposed by the project owner/operator, through persuasion or other means, in the absence of specific contractual authorities to direct or approve/disapprove actions

2. Considerations for Joint Ownership of Resource Installed Capacity

Any resource proposal in which BPA is offered a share amounting to less than half of a generating project must be reviewed with special care in order

to minimize BPA's risk exposure. This is even more critical where BPA has a minority interest. As a minority participant in the project, BPA needs to assure that its interests in such a project are sufficiently protected. BPA would expect that an acquisition contract governing such a transaction would contain provisions identifying specific decisionmaking criteria and procedures that may be anticipated for the term of the contract and provisions protecting BPA's financial exposure in such a project.

3. General Contract Management Objectives

BPA expects to be involved in all aspects of the owner/operator planning process, including the development of program objectives, implementation, and budgeting. In monitoring program expenditures, BPA expects that the owner/operator organization will be able to demonstrate that planned activities are being accomplished within the defined budget. BPA plans to use measurable (technical) performance factors for integration with financial objectives as a practical way of evaluating work performed in conjunction with any given project.

BPA's objectives in this process are:

- To ascertain the effect of proposed owner/operator near-term and long-term budgets on BPA's established rates and future rate stability
- To avoid detailed cost-based purchases where (1) disputes are bound to arise, and (2) incentives for cost control are not present; if this cannot be avoided, to gain requisite ownership rights to direct construction/operation in a prudent manner
- To gain total flexibility in the ability to adjust project construction and operation schedules, for maximizing BPA's ability to serve its firm obligations at the lowest cost to its customers
- To gain the right to unilaterally terminate our contract with sole discretion
- To ensure that audits of the owner/operator, and its contractors and subcontractors, can be and are performed on any designated item
- To establish appropriate and regular BPA-owner/operator mechanisms, processes, or procedures in the project agreement that ensure full airing and expeditious staff work on the resolution of project issues
- To gain the unilateral right to approve or disapprove the selection or continuation of the project manager
- To gain prior agreement on allowable overhead costs and formulas for distributing indirect charges, including mechanisms for changing such formulas, as warranted by circumstances
- To gain prior agreement in the allocation of shared costs, including mechanisms for changing such allocations as appropriate for multiple unit situations

- To ensure that all offers, offer evaluations, and proposed contract awards shall receive BPA approval prior to the awarding of such contracts

- To gain the right to maintain BPA representatives at project sites during project construction, operation, and decommissioning with free and open access to information as BPA deems necessary

- To ensure that owner/operators provide for BPA approval, on a yearly basis, an updated construction budget, and, on a timely basis, revised construction budgets reflecting substantial changes in construction plans, schedules, specification, and/or costs (projections will estimate five out-years of data, including rolling cash flows)

- To gain the right to require, on a discretionary basis, financial information, such as updated project budget forecasts, cash flows, and cost-to-complete estimates

- To ensure that owner/operators provide for BPA approval, any plans for replacement, repair, or betterment of capital expenditures as requested by BPA

- To ensure that owner/operators provide BPA with the prior opportunity for disapproving any expenditure or obligation of funds for capital additions, excepting funding for such additions as are mandated by governmental agencies for the purpose of meeting safety or regulatory requirements (in such cases, however, owner/operators must provide BPA with prior notification of such requirements and proposed compliance options)