

Competitive Procurement of Retail Electricity Supply: Recent Trends in State Policies and Utility Practices

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Background: Study of Recent Trends in Competitive Procurements

- Analysis Group was asked by NARUC and FERC to perform a study of current policies and practices for competitive procurements.
- Focus of study is upon states that have formally adopted policies or guidelines for competitive procurements.
- Research included:
 - Survey of state commission staff on policies and practices in competitive procurements within the state
 - Review of literature on procurements, including PUC orders and utility RFPs
- Analysis Group's research has been summarized in the report:

***“Competitive Procurement of Retail Electricity Supply:
Recent Trends in State Policies and Utility Practices” (July 2008)***

<http://procurement.webexworkspace.com/login.asp?loc=&link=>

Background: What the study does and does not cover

- **Our focus: The 40% of the states with formal policy (law or regulations) requiring use of competitive procurements**
 - Many states with traditional regulatory structures have recently adopted policy.
 - Most states in restructured electricity markets rely on competitive procurements.
- **Caveats:**
 - We make no recommendations for what policies a state *should* adopt.
 - We do not review practices and policies of:
 - Publicly owned utilities.
 - Very small investor-owned utilities.
 - Competitive suppliers or load serving entities (e.g., ERCOT Texas).
 - We do not focus on the details in states with open dockets.
 - We do not focus on FERC standards for reviewing wholesale PPAs..

Recognizing “Best Practices” – Core Criteria for Competitive Procurements

Applying these
criteria evenly is
harder than it would
seem.

<i>Procurements should be:</i>	
Fair and Objective	Affects the selection of best offers and thereby the quality of participation, thus a competitive response
Designed to encourage robust competition	Is supported through provision of adequate information to bidders, and reliance on appropriate safeguards and protections
Built on relevant and accurate price and non-price factors	Depends upon identification of sound evaluation criteria and methods, and reliance on them in practice
Administered in an efficient and timely manner	Depends on avoiding unnecessary administrative delays and burdens
Supported by PUC processes aligned with competitive response and outcomes	Relies on having PUC practices and decisions that encourage competitive response and attractive results for consumers

Frameworks for the Procurement of Electricity Supply for Retail Customers

Frameworks for Procurement of Electricity Supply for Retail Customers				
Electric Industry Structure	Divestiture of Plants	Procurement Framework / Product Solicited	Supply Portfolio Management	State Examples
Traditional	None	Incremental Supply – typically for resources from a power plant obtained through RFPs	Utility	CO, GA, LA, OK
Restructured, No Retail Choice	None or Partial	Incremental Supply (via RFP)	Utility	CA, MT
Restructured, with Retail Choice	Full (or near full)	Full Requirements Service (“FRS”) – via auctions or RFPs to provide retail supply for basic service customers	Market	MA, MD, ME, NJ
		Hybrid FRS Frameworks: <ul style="list-style-type: none"> • Long-term contracts (with FRS) • Some portfolio management functions • Role of public power authority • Specialized procurements (e.g., RECs) 	Variously Assigned to Market and to Utility	CT, DE, IL, OH, PA

Two Key Types of Procurements within These Frameworks

- **Incremental resource procurements**
 - Relied upon by utilities with (a) a resource portfolio and (b) responsibility for adding incremental resources as needed.
- **Full requirements service (“FRS”) procurements**
 - Relied upon by utilities that have (a) past generation divestitures and (b) for serving “standard offer” retail customer needs.
- **Fundamental difference in these procurements**
 - Incremental Resources → resources differ along many dimensions
 - FRS → standardized product & “price-only” evaluation

We discuss the two types of procurement approaches:

Incremental Resource Procurements - Overview

- **Used in states with traditional industry structure**
 - **The utility is responsible for adding incremental resources.**
 - **Competitive procurement policies have evolved in recent years.**
 - **Procurement may target particular types of resources – e.g.,**
 - **Baseload; load-following; peaking; new generation capacity.**
 - **All fuels; renewables; energy efficiency; demand response.**
- **Some states have more experience than others:**
 - **Arizona, California, Colorado, Florida, Louisiana, Montana, Oklahoma, Oregon, Utah, Washington.**
- **Most of these states either allow or require:**
 - **Utility self-build proposals.**
 - **Utility affiliates' participation in the RFP.**

Incremental Resource Procurements – Self-Dealing

A key challenge for regulators in incremental resource procurements is designing safeguards to prevent potential improper self-dealing by the utility.

- **In our report,**
 - **“Improper self-dealing” = the utility has dual roles of (a) evaluator and selector of winning bids, and (b) competitor, and the utility selects its own proposal as a result of a procurement intended or carried out to unduly favor its own proposal or the proposal of an affiliate.**
 - **“Proper self-dealing” = the utility has dual roles (evaluator/selector, and competitor) and selects its own proposal after fair and objective evaluation.**

Design of Sufficient Safeguards to Prevent Improper Self-Dealing

Structural/design issues to ensure that winning bids are chosen based on a fair and objective process to avoid improper self-dealing:

- **Commission review of RFP instruments and oversight of RFP procedures;**
- **Codes of conduct;**
- **Engagement of an independent monitor (“IM”);**
- **Public participation (e.g., comment periods);**
- **Information transparency (e.g., information requirements for RFP’s);**
- **Protection of commercially sensitive confidential information.**

Incremental Resource Procurements – Transmission (1)

Transmission impacts associated with particular incremental resource additions can vary considerably from one proposal to another.

- **Interconnection costs – direct costs to connect the facility to the grid**
- **Integration costs – direct and indirect costs to upgrade the transmission system if needed**
- **Congestion costs – costs associated with out-of-merit-order dispatch**

In comparing the value of incremental supply offers to retail customers, utilities must examine both these direct costs plus these transmission-related costs

Incremental Resource Procurements – Transmission (2)

Utilities should aim to find efficient and timely ways to obtain estimates of these costs to assist

- **prospective bidders (in submitting competitive offers)**
- **regulators (in reviewing utility evaluations of offers)**
- **utilities (in evaluating offers)**

Other important transmission cost issues:

- **Identification of transmission-related costs to include in offer review**
- **Bidder information on transmission costs**
- **Bidder assumptions about who pays for winner's system integration costs**
- **Comparability of transmission-related costs**

Incremental Resource Procurements – Economic & Financial Risks

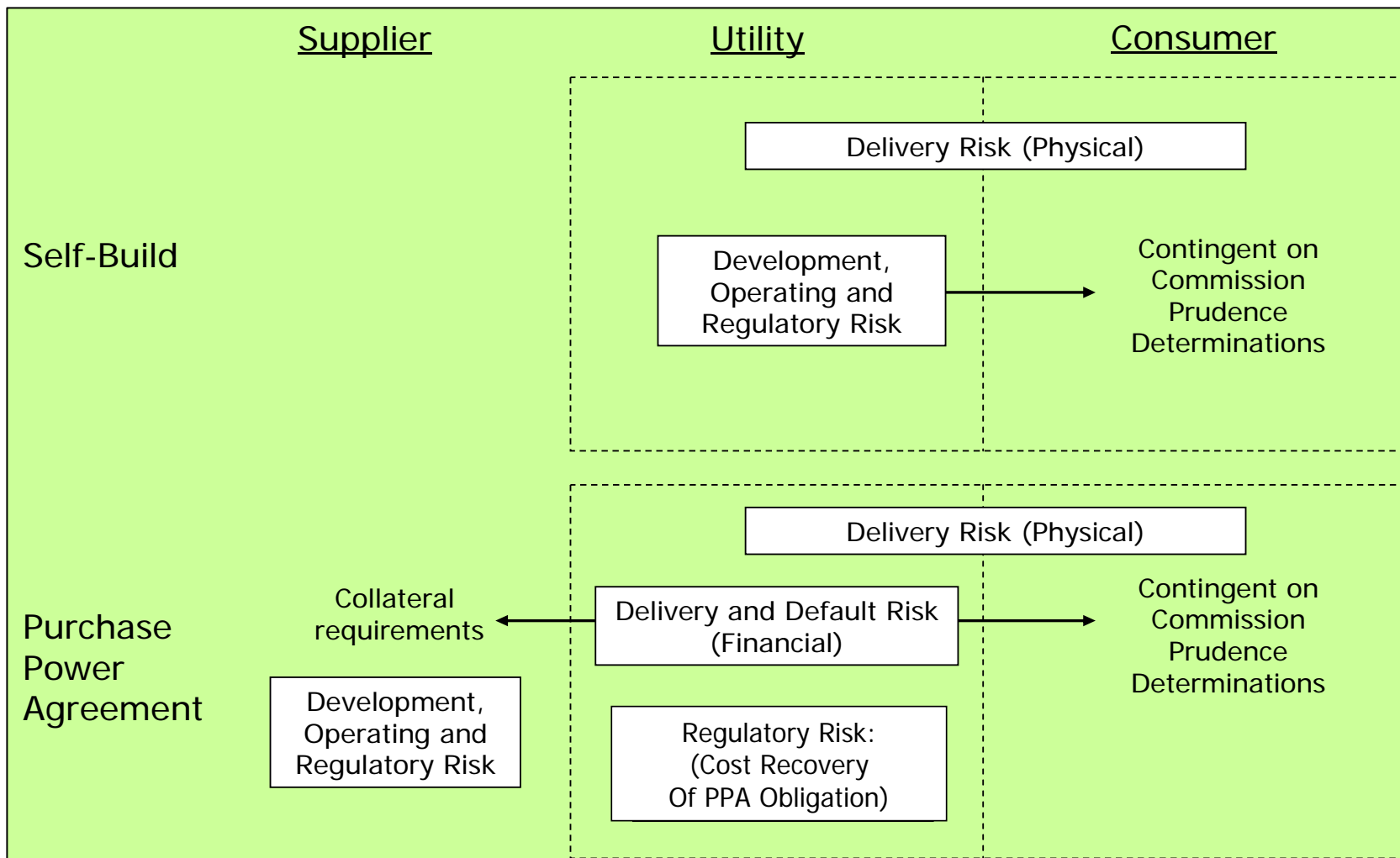
Different “deal structure” can impact distribution of financial risks between power supplier(s), the utility, and customers – and complicate identifying “best” offers for customers.

- **Key factors affecting the magnitude and distribution of these risks:**
 - **Buyer and seller obligations/responsibilities under PPA;**
 - **Commission prudence and cost-recovery determinations;**
 - **The inherent risks associated with different resource types;**
 - **The development status of power plant projects.**

Offer evaluations should aim to account for the allocation of all risks, but doing so complicates evaluations:

- **Many uncertainties are difficult to quantify;**
- **Financial risks vary with attributes of offers (e.g., technology);**
- **Contract terms may not fully capture risks to system reliability.**

Incremental Resource Procurements – Economic & Financial Risks



Incremental Resource Procurements – Debt Equivalency (1)

Concern: impacts of PPAs on utilities' financial risks:

- **Utility contractual obligations to supplier may create a financial risk for the utility if this obligation is not matched with a correspondingly firm expectation about PPA cost recovery.**
- **Since PPA costs are typically recovered as an expense, a PPA denies the utility an opportunity to earn a financial return – giving rise to:**
 - **The utility's concerns about the effects on earnings, capital structure (for ratemaking), and capital structure (for financial books);**
 - **Incentives for improper self-dealing.**
- **Different views exist on these risks – but with little empirical evidence about impacts.**
 - **Credit rating agencies have described certain quantitative balance sheet adjustments made for PPAs ...**
 - **... while noting that these are only one among many possible adjustments that may affect a utility's credit rating.**

Incremental Resource Procurements – Debt Equivalency (2)

Two basic approaches to addressing these issues – although still evolving:

- **During rate-case reviews of cost-of-capital and capital structure.**
 - **e.g., Colorado, Florida, Wisconsin**
- **In procurements, through use of adders to 3rd-party offers.**
 - **e.g., Louisiana, Washington**
- **California recently switched from using adders to possible rate-case reviews.**

Given the uncertainty about how PPAs affect utility financial risk:

- **Caution against assessing debt equivalency outside of a comprehensive evaluation that accounts for all various risks posed by alternative utility obligations;**
- **These issues are normally addressed in general rate case; doing so in procurements requires special Commission oversight.**

Full-Requirement Service Supply Procurements

FRS procurements are often used in states with restructured electricity markets.

- **“Price-only” design reduces evaluation and regulatory challenges:**
 - **Eliminates subjectivity (e.g., non-price criteria) and complexity of evaluation**
 - **Reduces opportunities for improper self-dealing**
 - **Safeguards may include independent monitors, code-of-conduct requirements, and various means to deter outright bid rigging**
- **“Price-only” design shifts risks from the utility to suppliers**
 - **Portfolio risk of constructing mix of supply agreements**
 - **Volumetric risk of growing demand or customer migration**

Final Thoughts and Conclusions

Evolution of the Means of Providing Retail Supplies in States Currently Relying on FRS Supply Procurements

Some states that currently rely (almost) exclusively on FRS procurements for retail supplies are undertaking or considering policy changes with potentially important implications for competitive procurements.

- **Utility participation in resource procurements (e.g., CT, OH)**
- **Utility procurement of resource portfolio (e.g., DE)**
- **Long-term contracts (e.g., MA, ME)**
- **Government involvement in procurements (e.g., IL)**
- **Procurement of renewable or alternative energy attribute credits (e.g., NY, PA)**

These policies are still evolving and regulators need to carefully consider their implications for resource procurements

- **Potential for increased reliance on incremental resource procurements**
- **These changes may also affect future FRS procurements**

Incremental Resource Procurements – Special Technology Challenges

Challenges of capital-intensive technologies (e.g., advanced technologies):

- **Most recent RFPs have resulted in PPAs for natural gas-fired facilities.**
- **Recent experiences with using procurements for baseload resources have varied, leading in some cases to requests for exemptions or specific RFPs for baseload projects.**
- **Advanced technologies pose special risks:**
 - **Greater technology uncertainty – with difficulty obtaining equipment performance guarantees or EPC contracts.**
- **Proper or improper self-dealing:**
 - **The opportunities for potentially large ratebase additions introduces incentives for utilities to shield such projects from competition even in situations where market processes are applicable.**

These issues are outside the scope of this report:

- **We encourage regulators and the industry to continue to examine these issues elsewhere.**

Conclusion – Final Thoughts

- **Experience to date:**
 - **There is now considerable experience in *designing* competitive procurements.**
 - **Actual experience with procurement *implementation* is somewhat more limited.**
 - **This is still a “work in progress.”**
 - **Many states are finding competitive procurements to be an essential tool for obtaining electricity supply that nonetheless introduces significant implementation challenges.**
 - **How regulators and utilities address the fundamental issues and important details are critical to their success.**

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To be discussed if there is time

Appendix Slides

**Recent Changes in State Policy
Regarding Competitive Procurement of Incremental Resources**

To be discussed if there is time

Recent Changes in State Policy Requirements Involving Competitive Procurements for Incremental Resources		
State	Date	Docket Name
Arizona	2007	Recommended Best Practices for Procurement (ACC Decision No. 70032)
California	2003 - present	Energy Action Plan, PUC Decision 04-01-050, AB57 and various other rulings
Florida	2002	Rule 25-22.082 Amended
Georgia	2004	Amendment to Georgia Code 515-3-4-.04 Identification of Capacity Resources
Louisiana	2004	Market Based Mechanism Order (General Order, Docket No. R-26172 Sub Docket A)
Oklahoma	2007	Title OCC, Subchapter 35: Electric Utilities – Amendments, Competitive Procurements
Oregon	2006	PUC Order No. 06-446
Utah	2005	Utah Energy Resource Procurement Act Statute (Title 54, Chapter 17)
	2007	Rules R746-420, R746-430, R746-440
Washington	2003	General Order No. R-509

To be discussed if there is time

Regulators' Checklist (1)

Table 2 Critical Issues in Designing Competitive Procurements for Incremental Supplies	
Commission Choices	Additional Considerations
Procurement Process Architecture	
Form of the commission's policy:	What form and in what level of detail will the Commission's policy take: e.g., Regulations? Informal guidelines? Decisions in response to utility proposals?
Role of an integrated resource plan ("IRP"):	What role will an IRP play in determining the timing, amount and type of resources to be procured through a competitive solicitation?
Product definition:	What is the product being procured? Will it be broadly or narrowly defined? Will demand-side offers be considered? How will any policy preferences for particular types of resources (e.g., renewables) be established and implemented?
Procurement procedures:	What requirements will be put in place: e.g., for requests for proposals ("RFPs"), auctions, negotiations, and other design details?
Involvement of an independent monitor:	Under what circumstances will an independent monitor or evaluator be required? Who chooses it? What actions and responsibilities does it undertake?
Commission staff's role:	Will the staff directly oversee the RFP process, on-site with the utility? Will the staff assist the oversight of an independent monitor?
Commission approvals:	At what stage(s) of the process does the Commission carry out a formal review and/or approval? E.g., approval of the IRP? The RFP design? The bidder short-list? Winning offers? Contract approval? Will the Commission's review of the process elements as implemented allow the Commission to endorse the contracts that result from it (assuming a finding that the process produced a competitive result)?
Public participation:	What parts of the process should include public participation? E.g., determination of the types of resources to be procured? Review of RFP instrument and/or model contract?
Scheduling process elements:	How will the timing of the process be designed to balance market and regulatory requirements?
RFP documents:	What materials will be issued with the RFP? E.g., evaluation criteria and weights? Model contracts? Credit and collateral requirements?
Pricing offers:	Will the initial bids involve final offer prices or preliminary indicative offers? Will bidders be permitted to "refresh" their offers over time during the RFP?

To be discussed if there is time

Regulators' Checklist (2)

Table 2 Critical Issues in Designing Competitive Procurements for Incremental Supplies	
Commission Choices	Additional Considerations
Evaluation of Offers	
Evaluation methods and criteria:	How will the array of price and non-price elements (e.g., location, resource operating characteristics, development status) of the offers be evaluated?
Comparison of offers with different risk profiles:	How will the evaluation compare offers with different assignments of various risks (e.g., fuel price risk, fuel supply deliverability, project development, construction cost, availability, credit risk, technology risk, changes in law)?
Transmission impacts and costs of any transmission upgrades:	How will the transmission-related cost implications of different offers be evaluated: Through the status of interconnection requirements? The costs of needed transmission system upgrades? Congestion impacts from dispatch of the proposed offer?
Evaluation of system interactions of offers:	How will the evaluation of offers assess interactions with the rest of the utility's portfolio (e.g., sensitivity analyses of key assumptions, such as fuel price changes)?
Debt equivalency:	Will the process consider the financial impact on the utility of contracts versus rate base investment? If so, how? E.g., using an adder assigned to offers from third parties in the RFP process? As part of the review of the utility's cost of capital in rate cases?

To be discussed if there is time

Key Procurement Policy Issues – A Checklist for Regulators (1)

Threshold	Second Order Question	Observation:
<p><input checked="" type="checkbox"/> Should the utility test the market for alternatives to building its own power plants?</p>	<p>➔ If so, does the commission require (formally) the utility to carry out a competitive procurement, encourage such procurements by providing specific guidelines or recommendations, or give the utility full discretion to do so?</p>	<p>Clarifying commission policy toward competitive procurement and making such policy statements easy to find in PUC websites may lower barriers to entry for independent suppliers seeking to participate in the state's market; on balance, this may serve to support a deeper response to any solicitations.</p>
<p><input checked="" type="checkbox"/> What is the "product" that the utility should procure through competitive solicitations?</p>	<p>➔ Is the procurement designed to solicit narrowly or broadly defined products? That is, should the procurement solicit offers for any type of resources to meet given power supply needs, or limit offers to:</p> <ul style="list-style-type: none"> ○ Supply-side resources? ○ Resources using a particular technology (e.g., renewables) or particular fuel (e.g., coal)? ○ Resources providing a particular function in a supply portfolio (e.g., baseload v. peaking)? ○ Capacity resources? ○ Resources in a particular zone? ○ Resources from new facilities? ○ Products satisfying particular regulatory requirements (e.g., renewable energy credits)? 	<p>Procurements with more narrowly defined products will allow greater reliance on price and less reliance on other evaluative criteria, although it may limit the depth of the market response and the creativity of offers from market participants. The greater control the commission wishes to exert over the choice of attributes of the product being solicited (e.g., type of resource, location, fuel or technology type, function in the portfolio), the more the commission will likely need to encourage review of formal (or informal) utility long-range resource plans in advance of the resource procurement.</p>

To be discussed if there is time

Key Procurement Policy Issues – A Checklist for Regulators (2)

Threshold Question	Second Order Question	Observation:
<p><input checked="" type="checkbox"/> Does the commission want to allow – or require – the utility to participate in the solicitation, either directly as a supplier proposing a resource relying upon regulated investment, or indirectly through a competitive affiliate?</p>	<p>➡ If so, what safeguards will the commission establish and enforce in order to prevent improper self-dealing to assure a fair and competitive solicitation, increase the opportunity for the best resource to be selected, and assure the market that there will be no improper preferential treatment of utility or affiliate offers (thus instilling confidence in the overall design of the competitive procurement)?</p> <p>➡ Whether or not the utility is allowed to or does participate in the solicitation, how will the commission ensure that the utility's evaluation is focused on decisions supporting lowest-cost, reliable service to customers, even where different resource choices may have different impacts on the utility's own real or perceived financial interests? For example,</p> <ul style="list-style-type: none"> ○ Implications for the utility's risk profile, capital costs, balance sheet, and so forth, associated with of a third-party contract versus investment a utility owned plant? ○ Implications for the performance of the utility's own plants (e.g., implications for stranded investment) from transmission congestion due to new resource additions? <p>➡ What guidance will the commission provide to the utility and to market participants about how various risks should be assigned in contracts between:</p> <ul style="list-style-type: none"> ○ The utility (as buyer) and a third party supplier, and in turn between the utility and its retail customers; ○ The utility as a power plant owner and its customers. 	<p>Putting in place appropriate safeguards to ensure that the utility's decisions are made with the interests of customer benefits and costs in mind involves great care in the overall design, implementation and supervision of the procurement. Key safeguards to guard against improper self-dealing include:</p> <ul style="list-style-type: none"> ▪ Use of an independent monitor throughout all phases of the process; ▪ Commission review of product definition, evaluation assumptions and techniques, contract terms and conditions, debt-equivalency issues in rate cases (not RFPs) and other elements to support fairness for market participants; ▪ Requiring comparable forms of risk mitigation in utility and non-utility offers, such as comparable treatment of offer "refreshing" and various types of risk, including development and construction risk, power plant performance risk, fuel price risk, and risks tied to changes in law or regulation, such as costs of mitigating carbon emissions.

To be discussed if there is time

Key Procurement Policy Issues – A Checklist for Regulators (3)

Threshold Question	Second Order Question	Observation:
<p><input checked="" type="checkbox"/> To what extent will winning resources be selected on price terms and non-price characteristics, some of which may be difficult to quantify and compare?</p>	<p>➤ How will the commission's policies shape how and what types of non-price characteristics should be considered by the utility in evaluating offers, in light of such criteria as:</p> <ul style="list-style-type: none"> ○ The potential differences in the importance of various non-price characteristics in alternative offers; ○ The potential for evaluation of non-price characteristics to impose high administrative costs or slow evaluation procedures; ○ The potential introduction of subjectivity (with the opportunity for self-dealing) that non-price characteristics may create? <p>➤ If non-price factors are necessary to the selection of "best" resources, how will the commission encourage a process that provides sufficient information to the market (e.g., what factors matter, what weight will be assigned to them, and how they will be measured) without also limiting the utility's flexibility to use qualitative judgment in evaluating offers? For example,</p> <ul style="list-style-type: none"> ○ Where the winning offers will become part of the utility's resource mix and have network service, how will the need for transmission additions be evaluated, particularly if impacts differ substantially among offers and take time and other resources to fully evaluate? ○ How will the utility take into account the development status (e.g., types of permits in hand, construction completed) of resource options in ways that support competitive responses while fully accounting for significant differences in risks to consumers? ○ How will the process incorporate any non-price factors that are relatively easy to put into dollar terms (e.g., transmission enhancement costs), and those (such as project development risk) which are harder to monetize? 	<p>The more transparent the evaluation procedures and criteria are to market participants, the more likely they will be assured that the evaluation process will be fair and objective. At the same time, the more the choice of "best resource" depends upon each offer's interaction with the rest of the utility's portfolio, the more the selection will depend upon complex modeling of the utility's portfolio; reliance on these models raises traditional transparency issues associated with "black box" modeling. As a result, regulators will need to pay attention to the modeling assumptions and inputs used by the utility in evaluating resource options (including sensitivity analyses) to help ensure a competitive result. Such review is particularly important where the utility (directly or indirectly) has a financial interest in the outcome of the results (e.g., either directly, if proposing a competing project, or more indirectly, if it owns another existing plant that may become less valuable depending on facility selection).</p>

To be discussed if there is time

Key Procurement Policy Issues – A Checklist for Regulators (4)

Threshold Question	Second Order Question	Observation:
<p><input checked="" type="checkbox"/> If you have committed to having your regulated utilities use competitive procurement processes, are you willing to align your own regulatory practices to support them?</p>	<p>➔ Assuming that markets assign risk to uncertain regulatory outcomes, how will the commission arrange – and commit to implementing and enforcing – its own actions to support outcomes that appropriately balance risks between suppliers, the utility and ratepayers? Relevant regulatory risks that can show up in price premiums include:</p> <ul style="list-style-type: none"> ○ Uncertainty about cost-recovery for utilities' contracts with power suppliers versus the utility's own investment; ○ Uncertainty about how long contract approval will take; ○ Uncertainty about whether the regulator will enforce the rules requiring fairness and objective processes; ○ Uncertainty about whether the commission will reopen the process – or throw out the results – if it doesn't like the particular outcome of a solicitation; and ○ Uncertainty about whether the regulator will allow the utility to take actions that circumvent the procurement, alter procurement procedures mid-stream, or dissolve the procurement (irrespective of rationale)? 	<p>The higher the market's confidence that the regulatory agency will support its own past policies and decisions, the lower the risk premium that will be built into offers from the market. Past commission policies and decisions may include meeting certain procedural time requirements to which it has committed and enforcing as appropriate any procurement rules previously adopted.</p>

To be discussed if there is time

Incremental Resource Procurements – Common Design Elements

Most incremental resource procurements involve the following basic components, in which the utility:

- Identifies needed resources (e.g., via a long-range IRP)
- Designs an RFP instrument to solicit offers (with public comment)
- Receives bids in response to a final RFP from interested suppliers
- Evaluates all offers and selects a winning offer, in either:
 - a single phase process, or
 - multiple stage process (e.g., pre-bid qualifications; short-list; final award group)
- Informs bidders and regulators of resource selections
- Enters into contract negotiations with the final award group
- Submits the results of the process (e.g., the award group with winning contracts) to the Commission for approval

To be discussed if there is time

Incremental Resource Procurements – Role of Resource Plans

Utility plans sometimes used to identify the electric product(s) to be procured:

- **Broad product definitions – allowing the market to propose options.**
 - The wider the range, the more likely a utility will need to compare price and non-price features among offers that may differ along many dimensions.
 - This inevitably introduces subjectivity into bid evaluation ...
 - ... but allows for creativity from the market.
- **Narrow product definitions:**
 - Reduce evaluation challenges ...
 - ... but risk producing results from the market that differ from the assumptions used in the IRP process (which relies on hypothetical resource estimates).

To be discussed if there is time

Incremental Resource Procurements – Evaluation Process Design

Evaluation Timing – Trade-offs:

- **Aim to minimize the time between submission of offers and awarding of contracts**
 - Reduces supplier's financial risk from the requirements that they honor initial contract terms;
 - Likely to encourage offers with lower prices.
- **Evaluation of incremental resource offers is highly complex and time consuming (need for multiple stages of analysis, complex production simulation modeling, etc.) ...**
 - ... thus, a hurried evaluation may result in poor resource choices.

To be discussed if there is time

Incremental Resource Offers – Other Structural Mechanisms for Oversight

Public (or Stakeholder) Participation

- Can occur in any stage of a procurement process;
- Public participation in early phases may avoid later disputes, delays.

Utility Codes of Conduct

- “Codes of conduct” address interactions between utility employees:
 - Team developing utility self-build proposals,
 - Team evaluating competitive offers,
 - Team administering utility transmission functions.
- “Codes of conduct” can reduce the likelihood that:
 - Bid evaluation team bias decisions in favor of utility/affiliate proposals,
 - Teams developing utility/affiliate offers have advantageous access to confidential information.

To be discussed if there is time

Incremental Resource Procurements – Contract Negotiation

- **Trade-offs in Allowing Negotiations:**
 - Allowing broad negotiations after offer selection may reduce procurement transparency and creates incentive to understate initial offers, but allows consideration of modifications that may increase benefits.
- **Bid “refreshing”**
 - Creates a tradeoff between incentive for accurate initial bids and reducing financial risks from stale offers;
 - Holding utility and third-party offers to the same “refreshing” rules reduces risk discrepancies.
- **Model Contracts**
 - Can provide guidance about the utility’s preferred terms and conditions.
 - Rules for proposing modifications should be clear – importance of common understanding across bidders.

To be discussed if there is time

Incremental Resource Procurements – Economic Risk

As previously discussed, PPAs and self-build offers results in important differences in the distribution of financial risks.

- Under a utility self-build, actual costs are not determined until after the procurement → consumers assume the risk for cost increases.
- By contrast, under PPAs, suppliers – not consumers – take on the risk that actual costs are higher than anticipated
- Thus, PPAs provide risk mitigation to consumers.
- At present, procurements do not generally account for this transfer of risk.
- Options to account for these risks include:
 - Quantitative adjustments
 - Payments tied to market indices
 - Utility agreement not to pursue recovery of cost increases

To be discussed if there is time

Differences in FRS Procurements Arise in Some Important Details

Product Definition

- **Regulators efforts to mitigate rate volatility arising from FRS procurements**
 - **Increase the FRS contract duration – longer-term contracts reduce price volatility by reducing purchase frequency.**
 - **Pool or average procurements over time by procuring only a portion of load in each procurement.**
 - **Specify pricing terms offered to customers (and procured from suppliers)**
 - Flat, non-varying or vary by hour, day, or season
- **Mitigating price volatility poses competing policy tradeoffs**
 - **Shield consumers from undesirable economic consequences,**
 - **... but, also slow the development of competitive retail markets**
 - **prevent customers from seeing the true cost of supplying power**
- **Residential products typically designed to provide more mitigation of rate volatility than industrial / large commercial products**

To be discussed if there is time

Differences in FRS Procurements Arise in Some Important Details

PROCUREMENT APPROACH

- **Descending price clock auctions and sealed bid Requests for Proposals**
 - Most states rely on sealed bid RFPs, but some have used auctions (e.g., New Jersey, Illinois)
 - Choice reflects tradeoffs between performance, cost, and complexity
- **Indicative bids can provide a means of assessing likely procurement performance and developing initial prices (clock auctions)**
 - Such prices may be helpful in protecting against unanticipated, adverse procurement outcomes
- **Mitigating against undesirable procurement outcomes**
 - After the fact assessments (with use of indicative prices?)
 - Mechanisms (e.g., Maryland Price Anomaly Procedure)

To be discussed if there is time

Differences in FRS Procurements Arise in Some Important Details

Price Bidder Eligibility Requirements

- **FRS procurements rely upon eligibility and collateral requirements to ensure supplier “quality”**
 - **Ability to participate (and transact) in relevant electricity markets**
 - **Physical ownership of generation facilities is typically not a requirement**
 - **Credit-worthiness**

To be discussed if there is time

Differences in FRS Procurements Arise in Some Important Details

Price Bidder Collateral Requirements

- **Collateral**
 - **Ensuring the means and incentives to deliver FRS supplies**
 - **Insuring the utility and its customers against financial loss in the event of supplier default**
 - **Level of collateral is based on the quantity of supply offered and the supplier's credit-worthiness**
 - **Important that collateral requirements balance the utility's need to insure against default against the deterrence such requirements may have on supplier participation**

To be discussed if there is time

Differences in FRS Procurements Arise in Some Important Details

Independent Monitors (“IMs”)

- **IM’s are less critical to procurement success in FRS procurements than in incremental resource procurements**
- **Nonetheless, IM may play several important roles in FRS procurements**
 - **Review RFPs and related materials, oversee information distribution, and participate in public workshops**
 - **Monitor all procurement phases to ensure a fair and objective process**
 - **Report on the procurements results, including an assessment the procurement’s competitiveness**
 - **Provide feedback on potential modifications to procurement procedures**

To be discussed if there is time

Differences in FRS Procurements Arise in Some Important Details

Procurement Timing and Commission Approvals

- **FRS procurements generally aim to minimize the time between submission of bids and awarding of contracts.**
 - **Minimize suppliers' financial risks from potential changes in market conditions after they submit their bids**
 - **Minimize the risk premium that suppliers include in their offer**
 - **Create positive incentives for supplier participation**
- **In most cases, procurements decisions are finalized at least five days**

To be discussed if there is time

Differences in FRS Procurements Arise in Some Important Details

Confidentiality

- **Policies regarding confidentiality of bidder information reflect a tradeoff:**
 - **Benefits of transparency about the market's performance**
 - **Protection of valuable and commercially sensitive bidder information**
 - **Valuable information about bidding strategies**
 - **Avoid alerting financial markets about identity of winners**
- **Careful design can protect valuable information while maintaining benefits of transparency (e.g., delaying release of identity of winning bidders)**