D.P.U. 92-153

Petition of DLS Energy, Inc. filed with the Department of Public Utilities pursuant to 220 C.M.R. § 8.07(2) stating a complaint regarding the disqualification of its project proposal and the designation of the Award Group by Boston Edison Company of the Boston Edison Company RFP 3.

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I. INTRODUCTION

A. Procedural History

On June 24, 1992, DLS Energy, Inc. ("DLS") filed with the Department of Public Utilities ("Department") a petition[1] ("Petition") pursuant to 220 C.M.R. § 8.07(2), stating a complaint regarding the disqualification of its project proposal and Boston Edison Company's ("BECo's") designation of the Award Group for BECo's request for proposals ("RFP"), BECo's third RFP ("RFP 3"), from non-utility generators ("NUGs").[2] The Petition asked the Department to: (1) investigate BECo's disqualification of DLS' RFP 3 project proposal; (2) reinstate DLS' project proposal in the group of projects to be scored in RFP 3; and (3) order BECo to designate DLS as the sole member of the RFP 3 Award Group. On July 10, 1992, the Department issued an Order of Notice that: (1) set July 15, 1992 as the deadline for petitions for leave to intervene in this case; (2) established criteria for filing responses to the Petition; and (3) set July 24, 1992 as the deadline for filing any such responses.

On June 26, 1992, Altresco Financial, Inc. ("Altresco")[3] filed a petition for leave to intervene.[4] On July 10, 1992, the Attorney General of the Commonwealth of Massachusetts

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[1] DLS filed a supplement to its petition on July 2, 1992.

[2] A NUG is either a qualifying facility ("QF") or independent power producer ("IPP").

[3] Altresco submitted a proposal in response to RFP 3 to sell power from a 132 MW natural gas-fired combined cycle unit in Lynn, Massachusetts. On June 1, 1992, BECo identified Altresco Lynn as the sole winner of the solicitation.

[4] On June 26, 1992, Altresco also filed a motion for expedited treatment of this proceeding. Because of the extended duration of this case, this motion is now moot (see Tr. 1, at 12).

filed a notice of intervention pursuant to G.L. c. 12, § 11E. On July 15, 1992, CMS Generation Co. and Montvale Energy Associates, L.P. (jointly "CMS") filed a petition for leave to intervene.[5] On July 23, 1992, the Hearing Officer issued a ruling (1) denying the petitions to intervene of Altresco and CMS, while (2) granting Altresco limited participant status to address the legal issues raised in this docket. On July 24, 1992, Altresco appealed this ruling. By Order dated July 22, 1993, Altresco was granted full intervenor status in this proceeding. DLS Energy, Inc., D.P.U. 92-153-1 (1993).

On July 24, 1992, BECo filed its answer to DLS' Petition ("BECo Answer"), accompanied by a Memorandum opposing the Petition ("BECo Memorandum") and affidavits of William P. Killgoar ("Exh. BE-1") and John J. Reed ("Exh. BE-2"). Also on July 24, 1992, Altresco filed an answer supporting BECo's disqualification of DLS' proposal ("Altresco Answer").[6] On August 6, 1992, in accord with a July 30, 1992 Notice of Opportunity to file additional pleadings, DLS filed a Response to the Answers of BECo and Altresco ("DLS Response").

A technical session was held in this matter on September 16, 1992. On July 19, 1993, the Hearing Officer issued an Order of Notice that: (1) set July 29 and July 30, 1993 as hearing dates; (2) required BECo to score DLS' project proposal, without prejudice to any

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[5] CMS submitted a project proposal in RFP 3 and filed a petition with the Department, docketed as D.P.U. 92-166, stating a complaint regarding BECo's scoring of its project proposal. The Department issued an Order on August 31, 1993 denying CMS' petition.

[6] Also on July 24, 1992, Altresco filed a motion for summary judgment. Because of the Department's disposition in this case, the Department need not rule on the motion for summary judgment.

party, and revise, if necessary, the RFP 3 Award Group;[7] and (3) determined the scope of the proceedings. Hearings were held on July 29 and 30, 1993, at which certain testimony was taken under sealed transcript and certain exhibits[8] were given confidential treatment.[9] At the hearings, William P. Killgoar of BECo and John J. Reed of Reed Consulting Group ("RCG")[10] testified for BECo, while Daniel L. Smith of DLS testified for DLS.[11] On

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[7] On July 27, 1993, the scoring was submitted to the Department and given confidential and proprietary treatment. This scoring is not the subject of the instant proceeding and will not be addressed in this Order.

[8] In a July 30, 1992 Notice of Opportunity to File Additional Pleading, the Department indicated that no further pleadings would be accepted for filing unless otherwise directed or approved by the Department. No additional pleadings were authorized. Additionally, in a memorandum dated July 19, 1993, the Hearing Officer indicated that no new prefiled testimony or affidavits would be accepted by the Department. On July 27, 1993, DLS issued its First Set of Interrogatories and Request for Documents. BECo objected to DLS' discovery request on July 28, 1993, stating that the Hearing Officer's memorandum of July 19, 1993 did not provide for pre-hearing discovery. At the hearing, while maintaining its objection, BECo provided certain documents to DLS in response to its request for documents. During the hearing, DLS had the opportunity to request further documents from BECo in the form of Record Requests. All Record Requests made by DLS were granted. Therefore, the Department hereby sustains BECo's objection as to any discovery not provided at the hearing or in subsequent Record Requests.

[9] In this case, all of the exhibits (except BECo's RFP 3, Exhibit DLS-14), the record responses, and most of the transcripts are confidential. In order to fairly portray the positions of the parties and to show the bases for the Department's decision, the Department will characterize the data in these exhibits as they appear relevant, in such a way as to avoid revealing specific information which is proprietary.

[10] RCG provided consulting to BECo during the RFP 3 process.

[11] In a memorandum dated July 26, 1993, the Hearing Officer required the parties to submit a witness list. On July 28, 1993, in response to the witness list submitted by DLS, BECo objected to DLS's designation of witnesses. In particular, BECo objected to two witnesses from Besicorp. At the hearing, DLS sponsored only one witness, the President of DLS Energy, Inc. Due to the fact that DLS did not call the

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August 12, 1993, the Hearing Officer ruled on certain evidentiary objections and allowed the following exhibits into the record of this case: Exhibits BE-1 through BE-7 and Exhibits DLS-1 through DLS-11.[12] On August 11, 1993, DLS, BECo, and Altresco filed simultaneous briefs in this matter.

B. Background on BECo's RFP 3

Pursuant to an Order by the Department, BECo issued its RFP 3 on October 11, 1991.[13] By January 31, 1992, the response deadline for proposals in RFP 3, BECo received 41 project proposals for a total of 3,300 MW.

On May 20, 1992, BECo petitioned the Department to defer further activities in RFP 3 to its first integrated resource management proceeding, and in particular to defer announcing the Award Group and negotiating purchase power contracts with any Award Group members. Boston Edison Company, D.P.U. 92-130 (1992). On June 1, 1992, BECo announced that it had selected the Altresco Lynn project proposal as the sole member of the RFP 3 Award Group. On June 2, 1992, the Department ordered BECo to announce the Award Group but granted a temporary stay of BECo's obligation to negotiate and execute a

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[11](…continued)
witnesses to which BECo objected, and the fact that DLS's designation of witnesses was not argued by BECo at the hearing or on brief, the Department dismisses BECo's objection as moot.

[12] As no objections were received to Exhibits DLS-12 through DLS-15, these exhibits have also been entered into the record of this case.

[13] As issued, BECO's RFP 3 provided for a tentative supply block within the range of 132 to 306 megawatts ("MW"). Boston Edison Company, D.P.U. 90-270, at 35 (1991). The Department later set the size of the final supply block at 132 MW. Boston Edison Company, D.P.U. 90-270-C at 4 (1992).

purchase power contract with the RFP 3 Award Group. Boston Edison Company, D.P.U. 92-130-1, at 11, 13 (1992). During the following five weeks, DLS and five other project sponsors[14] submitted petitions to the Department, generally claiming that their bids were improperly scored or disqualified, thereby challenging BECo's designation of Altresco as the sole Award Group member. On August 4, 1992, the Department granted a further stay of BECo's obligation to negotiate and execute a purchase power contract with the RFP 3 Award Group until the Department issued a decision on BECo's petition to defer RFP 3. Boston Edison Company, D.P.U. 92-130-2 (1992).

On June 25, 1993, the Department issued an Order denying BECo's May 20, 1992 petition to defer further activities in RFP 3. Boston Edison Company, D.P.U. 92-130 (1993). The Department required BECo to begin negotiating a purchase power contract with the RFP 3 Award Group, but suspended BECo's obligation to execute a contract with the Award Group, until the Department issues final Orders in the proceedings involving challenges to the rankings in BECo's RFP 3. Id. at 33-34.

On June 30, 1993, BECo filed with the Department a motion for immediate stay of the Department's June 25, 1993 Order in D.P.U. 92-130. In an Order dated July 14, 1993, the Department denied this motion. Boston Edison Company, D.P.U. 92-130-A (1993). On

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[14] The four proceedings which addressed allegations of improper scoring were Concord Energy Corporation, D.P.U. 92-144; CMS Generating Company and Montvale Energy Associates, L.P., D.P.U. 92-166; Bio Development Corporation, D.P.U. 92-167; and Williams/Newcorp Generating Company, D.P.U. 92-146. Orders resolving those proceedings were issued on August 31, 1993. In addition, West Lynn Cogeneration filed a petition protesting BECo's decision in RFP 3 to disqualify its bid. This petition, docketed as D.P.U. 92-142, was withdrawn on May 19, 1993.

July 14, 1993, BECo filed an appeal of the Department's June 25, 1993 Order with the Massachusetts Supreme Judicial Court. As of the date of this Order, the Court has not yet ruled on the appeal.

C. Background on the DLS Disqualification Case

On January 31, 1992, DLS submitted a bid in response to RFP 3, proposing to construct a 306 MW facility in BECo's service territory (Exh. DLS-1, A-24). On May 19, 1992, BECo informed DLS that, pursuant to RFP 3 Section 3.8.1(n), it had disqualified the DLS project proposal because in BECo's judgment DLS would be unable to "fulfill the terms or conditions of the Project Proposal" (Exh. DLS-2, Tab A). BECo reaffirmed its disqualification decision by letter dated June 1, 1992 (id., Tab C). Section 3.8.1 of RFP 3, "Eligibility Requirements -- Basis for Disqualification," states that a project proposal may be disqualified for any one of fifteen specified reasons, including Section 3.8.1(n):

> Determination by BECo, with MDPU [Department] concurrence, that the Project Proposal does not represent a bona fide offer or that Sponsor will be unable to fulfill the terms or conditions of the Project Proposal.[15]

II. STANDARD OF REVIEW

The Department's regulations governing the purchase of power from NUGs state that if, "at any time, a qualifying facility is aggrieved by an action of a utility pursuant to these

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[15] The Department's General Counsel, in a March 19, 1992 letter to BECo, interpreted the phrase "with MDPU concurrence" in Section 3.8.1(n) of RFP 3 as not requiring prior Department approval of a disqualification based on that provision. The letter stated, in part, "[i]nstead, a reasonable interpretation of these words -- in the context of RFP 3 and the Department's general approach to RFP solicitations -- indicates that any project proponent disqualified by the Company pursuant to Section 3.8.1(n) could petition the Department to investigate the Company's actions under 220 C.M.R. § 8.07(2)."

regulations, the qualifying facility may petition the Department to investigate such action." 220 C.M.R. § 8.07(2). In reviewing any petitions filed pursuant to 220 C.M.R. § 8.07(2), the Department has applied a standard of "reasonableness." In Riverside Steam and Electric Company, D.P.U. 88-123, at 19-20 (1988) ("Riverside I"), the Department stated

> that the standard of reasonableness incorporates elements of fair dealing, due care, and good faith. These must be considered in the context of the transaction concerned and the relationship of the parties. In reviewing the utility's actions, the Department will not substitute its own judgment for that of the utility so long as there is a reasonable basis for the utility's actions. Thus the Department will impose appropriate remedies only if it finds that, given what the utility knew or should have known at the time, its actions have no reasonable basis. Under 220 C.M.R. § 8.07(2), the burden of proof is on the aggrieved QF.

See also Destec Energy et al., D.P.U. 92-46, at 4 (1992) ("Destec") (BECo's acceptance of bids submitted five to seven minutes late in RFP 3 found to be reasonable); EUA Power Corporation, D.P.U. 92-38, at 5 (1992) (BECo's determination that the petitioner's portion of Seabrook nuclear power station was not an IPP found to be reasonable); Riverside Steam and Electric Company, D.P.U. 88-123-B at 7 (1991) ("Riverside II") (utility's actions in a contract negotiation dispute found to be reasonable); and Boston Edison Company, D.P.U. 88-158, at 23 (1990) (reasonableness standard to be used to assess BECo's actions in refusing to enter into a new contract with a QF bidder). Compare MASSPOWER, Inc., D.P.U. 89-52, at 3 (1990) ("MASSPOWER") (BECo's disqualification in RFP 2 dispute found to be unreasonable where bid provisions were ambiguous and the bidder's pricing formula and escalation indices comported with the RFP); Wheelabrator Environmental Systems, Inc., D.P.U. 88-191, at 8 (1988) ("Wheelabrator") (utility's disqualification found to be unreasonable where decision was based on a bidder's failure to file Intent to Bid form).

The Department has stated that "[in] applying the standard of review established for this case, we must consider [the company's] actions taken as a whole and not simply score each action as reasonable or unreasonable." Riverside II at 61.

The Department also has stated that, in matters concerning an approved RFP, "the Department will allow an electric company a measure of discretion in administering and managing the RFP process." Destec at 13. In Destec, the Department explained that

> [a]llowing a measure of discretion at this stage in the RFP process is appropriate in light of the Department regulations [220 C.M.R. §§ 8.00 et seq.] governing other stages of the RFP process where explicit requirements for the content of an RFP and the solicitation and contracting are evident.... Thus, we consider that there are sufficient safeguards to allow an electric company broad discretion in the management of its approved RFP.

Id. at 13.

However, the electric utility's discretion in administering and managing the RFP process is not unlimited and is subject to Department review. For example, the Department has found that it is unreasonable for a utility to use a non-disqualification RFP provision (such as the requirement to file an Intent to Bid form) as the basis for disqualification, even though the RFP language was approved by the Department. Wheelabrator at 11. In MASSPOWER, the assessment of the reasonableness of a utility's decision to disqualify a project proposal submitted in response to an RFP required the Department "to review and interpret the requirements of the RFP to determine, first, whether MASSPOWER [the project sponsor] complied with the terms of the RFP, and second, whether any failure to comply with such terms warrants disqualification." MASSPOWER at 3. Thus, the Department examines whether the utility has applied a provision of an RFP consistent with its terms and

stated purpose. Furthermore, in cases where a bidder has been disqualified pursuant to a non-disqualification provision, the Department has stated that "only to the extent that the terms of the RFP are ambiguous will the Department look to the regulations, past Orders, statutes and policies to resolve the dispute." Id.

The Department also has indicated that the standard described above "would be considered and applied on a case-by-case basis, depending, in part, on the type of action complained of by the QF." Id., citing Riverside I. In Destec at 13-14, the Department indicated that an electric company must administer its RFP in a manner that prevents favoritism and treats all projects sponsors equitably. Finally, the Department has urged the utility companies, in the exercise of their discretion, to "construe [RFP] language liberally and reasonably, especially when considering threshold requirements that could result in a technical disqualification for an otherwise cost-effective project." MASSPOWER at 35.

III. POSITIONS OF THE PARTIES

A. Standard of Review

In this proceeding, the Department invited the parties to comment on the appropriate standard of review to be applied in this case (See Tr. 1, at 8).

1. BECo

Citing Riverside I, Destec, and MASSPOWER, BECo argues that DLS must prove that BECo had no reasonable basis for disqualifying the DLS proposal from RFP 3 (BECo Brief at 4-6). BECo contends that reasonableness must be judged by what BECo knew or reasonably should have known during the RFP 3 Review Period (id.). BECo emphasizes that a complaining bidder bears a heavy burden to overturn the facially reasonable judgment of a

utility (id. at 2). According to BECo, the complaining bidder "must show conclusively that the utility's decision was so unreasonable and so arbitrary that no reasonable justification is possible" (id.). Furthermore, BECo contends that, for fundamental policy reasons, the judgments made by a utility in managing its own RFP should be presumed reasonable until proven otherwise (id.). For example, BECo argues that if the Department re-decided matters based on each petition by a disgruntled bidder, the RFP process would become unworkable (id.).

2. DLS

DLS agrees that the standard to be applied in this case is one of "reasonableness" (DLS Brief at 5). DLS further argues that the Department has found that "rather than disqualifying a bid summarily, [a utility] has the obligation to evaluate the proposal and to reject the contract only if it is not cost-effective" (id. at 7, citing MASSPOWER at 30). DLS contends that, in assessing BECo's decision to disqualify its proposal, the Department "should review the RFP, BECo's obligations to treat all proposals equitably and the substantial harm to DLS and BECo's ratepayers resulting from the disqualification" (id. at 7). DLS differentiates Destec, observing that in Destec the petitioners failed to prove prejudice or harm to themselves or BECo's ratepayers, whereas DLS asserts that irreparable harm to DLS and BECo's ratepayers would result from the disqualification of DLS' proposal (id. at 6, 28).

3. Altresco

Citing Riverside I and other cases, Altresco argues that the relevant standard of review is whether BECo's actions were reasonable (Altresco Brief at 3). Altresco endorses

the policy that a utility should give the benefit of the doubt to a bid in a close call or with an ambiguous RFP requirement, when disqualification is at issue (id. at 13, citing MASSPOWER). Altresco asserts that only in cases where a utility has acted contrary to its RFP, or has interpreted an ambiguous provision of its RFP, has the Department found the utility to be unreasonable (id. at 5, 7). Altresco contends that Section 3.8.1(n) of RFP 3 is unambiguous and therefore the Department need look no further than the provisions of the RFP, since the Department has said it would look further only if the terms of an RFP are ambiguous (id. at 6, citing MASSPOWER at 3).

B. BECo's Review Process

1. BECo

BECo asserts that it consistently and equitably reviewed all project proposals submitted in response to RFP 3 (BECo Brief at 6). BECo indicates that an initial screening was performed to review project proposal scoring sheets and RFP 3 threshold criteria for obvious errors, and that the initial screening was followed by a closer review by a different group of BECo staff and by RCG consultants (id.). Internal memoranda noted certain pricing issues with the DLS proposal, and the DLS proposal was subsequently reviewed more closely by BECo and independently by RCG prior to disqualification (id.). In reaching its disqualification decision, BECo asserts that it relied on its own expertise and RCG's independent evaluation (id. at 14).

BECo contends that, in evaluating and disqualifying DLS, it strictly followed the provisions of RFP 3 concerning which documentation it was to consider and which documentation it was required to disregard (id. at 6, n.1, and at 9). BECo states that, in

evaluating projects pursuant to RFP 3: (1) BECo was obligated to consider only project documentation that was provided with a proposal (§ 4.3.4); (2) each project sponsor had the responsibility to provide all supporting bid documentation (§ 4.3.6(b)); and (3) BECo was entitled to, but not obliged to, seek clarification or verification of any material contained in a project proposal (§ 4.5.1(a)) (id. at 9-10). BECo asserts that it did not seek clarification or additional documentation from DLS because it did not find any ambiguities in the DLS bid (id. at 12).

BECo argues that it would have contravened the rules of RFP 3 if it had accepted and considered the supplemental information provided by DLS after the RFP 3 response deadline[16] (id. at 10). If supplemental information were accepted from bidders as a general matter, BECo claims that the RFP process would become inequitable and chaotic (id.).

2. DLS

DLS contends that the BECo review process was inadequate (DLS Brief at 2-4). DLS characterizes BECo's review as "disjointed", and contends that BECo "scrambled to justify its actions after the fact" (id. at 4). DLS argues that the witnesses made available by BECo for the hearing, BECo's Mr. Killgoar and RCG's Mr. Reed, lacked expertise or spent inadequate time in reviewing the DLS bid, and were not as involved in the evaluation of the DLS proposal as those persons (RCG's John Higgins, BECo's John Campanella and others)

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[16] In a March 24, 1992 letter, BECo replied to letters dated February 8, 1992 and March 6, 1992 from DLS, indicating that DLS' proposed changes in size (from 306 to 130 MW) and site were not acceptable, since such changes would be a basis for disqualification under Section 3.8.1(o) of RFP 3 (Tr. 2, at 200-201, citing Exhs. BE-5 and BE-6).

who were more involved in reviewing and evaluating the DLS proposal (id. at 2-4).[17]

DLS contends that BECo was required to seek clarification of issues raised by the DLS proposal prior to disqualifying it, but did not follow its own bid evaluation procedures, since BECo never requested clarification of DLS' proposal (id. at 11).[18] DLS asserts that during BECo's evaluation process, BECo contacted other proposal sponsors to seek clarification of their bids (id. at 10-11). DLS cites a memorandum from John Higgins of RCG to BECo, containing a list of questions concerning DLS' price and viability factors, contending that these were intended to gain clarification of DLS' project proposal (id. at 11, citing RR-DLS-3 at 9). DLS also cites handwritten notes by BECo's William Gray, dated February 11, 1992, which state: "looking for more documentation re: fuel arrangements" (id., citing Exh. DLS-12). Based on these two documents, DLS argues that some persons at BECo and RCG thought clarifications of the DLS proposal were required, but these persons were "obviously ignored" in BECo's review process (id. at 24).

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17 On brief, DLS argued that BECo failed to produce witnesses with the most knowledge of the relative facts (DLS Brief at 2-3). The Department notes that DLS had opportunity to request additional witnesses at the hearing, and that DLS did not object to BECo's designation of witnesses at the hearing or by motion after the hearing. If DLS was unsatisfied with the responses of BECo witnesses, it was incumbent on DLS to raise a timely objection, which DLS has failed to do.

18 DLS indicates that BECo met with DLS on May 28, 1993, after the disqualification decision, to allow DLS to explain its bid and ensure that BECo had not misunderstood the DLS bid (DLS Brief at 15, n.12). DLS argues that if there were a possibility that BECo had overlooked or misunderstood the DLS proposal, a pre-disqualification meeting would have been appropriate (id.). However, DLS asserts that "the meeting on May 28, 1992 was not an exchange but merely an opportunity for BECo to state after the fact that it had a meeting with DLS" (id.). DLS claims that BECo changed its position and cited four new reasons which it now claimed led to its conclusion that DLS would not be able to fulfill the terms and conditions of its proposal (id. at 15).

Nevertheless, DLS claims that it supplied BECo, between January 31, 1992 and June 1, 1992 (the "RFP 3 Review Period"), with clarifications in the form of supporting documentation containing information in sufficient detail to allow BECo to unequivocally confirm DLS' representations (id. at 29).

3. Altresco

Altresco claims that BECo conducted a fair and comprehensive review of the DLS bid prior to disqualification, involving a two-phase internal review and an independent evaluation by RCG (Altresco Brief at 8). Altresco also claims that BECo and RCG possessed the necessary expertise to evaluate the DLS bid, including various specialists and an extensive data base of project cost information from BECo's planned Edgar unit,[19] RFP 3 bids, and RCG's work for 50 developers on 200 projects (id. at 8-9, citing Tr. 2, at 39). Altresco argues that BECo reasonably relied on its own expertise to evaluate the DLS bid, and that supplemental information offered by DLS during the RFP 3 Review Period (Exhs. DLS-4 through DLS-11) about natural gas prices and vendor estimates of construction costs was already available to BECo and RCG, in the form of general market information (id. at 11).

Altresco contends that BECo's decision not to seek or review DLS' supplemental information was consistent with the terms of RFP 3, as approved by the Department, and with BECo's actual practice in evaluating other RFP 3 project proposals (id. at 10). Altresco cites RFP 3 in claiming that: (1) only representations made in the bid were to be considered

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[19] The Edgar unit, a 306 MW gas-fired combined cycle generating plant, was the avoidable unit used to calculate the ceiling prices in RFP 3. Boston Edison Company, D.P.U. 90-270, at 4, 32 (1991). In May 1993, BECo deferred the Edgar unit indefinitely (BECo Brief at 3).

in evaluation and ranking project proposals (§ 4.3.4); (2) the project sponsor was responsible for providing all necessary supporting documentation with its bid (§ 4.3.6(b)); and (3) BECo was under no obligation to solicit additional documentation if the submitted documentation was insufficient in BECo's judgment (§ 4.3.6(b)) (id.). Altresco asserts that BECo sought supplemental information from project sponsors only when an ambiguity in their bids existed, but that BECo found no ambiguities in the DLS bid (id. at 10, citing Tr. 2, at 109).

Altresco contends that DLS offered BECo certain supplemental information from various fuel and equipment suppliers, but that BECo was barred from accepting this information after the solicitation deadline, under Section 4.3.4 of RFP 3 (id. at 11, n.3, referring to Exhs. DLS-5 through DLS-9, DLS-11).

C. Fuel Costs

1. BECo

BECo contended that DLS based its "aggressive, fixed energy price" on a very qualified letter of intent, with the fuel price set on a "market sensitive basis," leading to potentially serious understatement of fuel costs (BECo Memorandum at 13). BECo argues that the fuel plan contained in the DLS bid was based solely on a January 28, 1992 letter ("January 28 Letter") between Energy Marketing Exchange, Inc. ("EME", a fuel brokerage firm) and DLS, which BECo characterizes as a letter of interest and not a letter of intent (BECo Brief at 13, citing Tr. 2, at 22, 75). BECo contends that DLS' pricing and transportation arrangements are "highly speculative", and that DLS failed to establish that it had firm gas arrangements at fixed prices (id. at 13, citing Tr. 2, at 24).

BECo claims that DLS' projected prices did not reflect market conditions and that the

arrangements cited in the January 28 Letter were not achievable (id. at 13-14, citing Tr. 2, at 24). BECo contended that the fuel price projection used by DLS in developing its price proposal was far below the gas price projections shown in RFP 3 or used in other recent NUG bids, and was unrealistically low (Exh. BE-2, at 4). BECo claimed that Canadian gas must pass through the TransCanada and Iroquois Pipelines to reach the Tennessee Pipeline, and that transportation rates for those two pipelines must be added to the Tennessee rate used in the DLS proposal (Exh. BE-4, at 2; Tr. 2, at 206-208). In addition, BECo maintained that if DLS were planning to bring gas up from the Gulf on the Tennessee Pipeline, the transportation rates are much higher than the transportation price assumed in the DLS proposal (Tr. 2, at 207).

BECo claimed that DLS inappropriately mixed a Lower Heating Value ("LHV") basis for plant heat rate with a Higher Heating Value ("HHV")[20] basis for natural gas prices, resulting in an eleven percent[21] understatement of its energy rate and consequently its fuel

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[20] LHV and HHV measure the heat available in a given amount of fuel. The two heating values, LHV and HHV, arise from the nature of the combustion process, combined with what happens to the combustion products. The combustion products of hydrocarbon fuels, such as oil and natural gas, are chiefly carbon dioxide and water. The LHV assumes that none of the water formed by combustion condenses into a liquid before it exits the system. The HHV assumes that all of the water formed condenses, adding the characteristic heat of condensation from water to the heat of combustion from the fuel.

BECo explained that corresponding LHV and HHV heat rates are defined for combustion equipment systems, in order to calculate the rate at which fuel is used to produce electric energy (Tr. 2, at 30). The heat content and price of fuels are commonly stated on an HHV basis, while equipment heat rates are commonly stated on both HHV and LHV bases (id.; Exh. DLS-1, Doc. 3, at 8-9).

[21] For natural gas (methane), the ratio of HHV to LHV is about 1.110.

use[22] (BECo Memorandum at 12-13; Exh. BE-1, at 10; Tr. 2, at 30-31, 216-218).

2. DLS

DLS argues that BECo's contention that DLS' fuel plan was based solely on a qualified, non-binding letter of intent is incorrect, and easily contradicted by supporting information supplied to BECo by DLS before its disqualification (DLS Brief at 16-18). DLS claims that, under principles of contract law, the fuel plan embodied in the January 28 Letter, submitted with its bid (Exh. DLS-2, Tab G at 2-3), represents a letter of intent and binding agreement between DLS and EME for EME to provide all of DLS' fuel needs at the price used in the DLS bid (DLS Brief at 17).[23] DLS contends that, if BECo had determined that the DLS fuel plan was ambiguous or lacked support, then this should have been reflected in BECo's scoring of the project proposal, as required in the RFP 3 scoring system, and should not have been a basis for disqualification (id. at 20).

DLS asserts that its fuel plan assumes specific gas costs based on favorable market

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22 Dividing the equipment's HHV heat rate by the fuel's HHV heat content yields the amount of fuel used to generate a given amount of electricity. Alternatively, dividing LHV heat rate by LHV heat content gives the same result, according to BECo (Tr. 2, at 30-31). Here, BECo contends that by dividing an understated (LHV) heat rate by the HHV heat content, DLS has underestimated the amount of fuel required for its facility (Tr. 2, at 216-217).

23 DLS argues that the binding nature of the agreement between EME and DLS was confirmed in a February 13, 1992 letter sent from EME to BECo (DLS Brief at 17-20, citing Exh. DLS-10). DLS also asserts that BECo received a letter from MidCon Marketing Corporation ("MidCon"), dated April 16, 1992, confirming the DLS project proposal fuel projections (id. at 20, citing Exh. DLS-11). DLS contends that both EME and MidCon are nationally known gas supply firms, and claims that BECo was aware, before DLS' disqualification, that both EME and MidCon substantiated the fuel plan projections in the DLS bid (id.).

conditions during the first quarter of 1992 (id. at 19-20). DLS submitted four documents from early 1992 to show that the fuel pricing in its bid is realistic and attainable:[24] Exhibit DLS-2, Tab G at 2-3, the January 28 Letter; Exhibits DLS-4 ("January 6 Letter"), DLS-10 ("February 13 Letter"), and DLS-11 (the April 16 "MidCon Letter"). The January 6 Letter from EME which DLS submitted to support its fuel plan describes BECo's gas price projections in RFP 3 as "conservative on the high side" (Exh. DLS-4).

DLS submitted the January 28 Letter from EME with its project proposal to support the fuel commodity price shown in its project proposal (Exh. DLS-2, Tab G at 2-3). The letter indicates that EME will sell gas[25] and No. 2 oil backup service to DLS on a daily basis, and provide transportation service to the facility (id.).[26] The letter specifies that gas

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[24] On August 11, 1993, DLS also submitted with its Brief a fifth document in support of its fuel pricing, eight pages from trade journals for January and February 1992. On August 16, 1993, BECo filed its Motion to Strike this information, claiming it was filed late and BECo had not had the opportunity to cross-examine DLS' witness on this information or to offer rebuttal information. The disputed pages contain selected gas price information of a type routinely available to BECo and the Department, from a small part of the RFP 3 Review Period. This information, while relevant, was available to all parties throughout the course of the proceeding, but without explanation for the delay was not timely presented by DLS to be subject to cross-examination and rebuttal testimony. It represents a view of market conditions over only the first four weeks of a nineteen week period, during which market conditions changed greatly. Accordingly, because these pages provide a one-sided view not subject to cross-examination and rebuttal, the Department rules that they shall not be admitted into evidence in this proceeding and hereby grants BECo's Motion to Strike.

[25] The gas would come from domestic and Canadian sources, using Tennessee Gas Transmission Company ("Tennessee"), Iroquois Gas Transmission Systems, L.P. ("Iroquois"), and other pipelines as necessary (Exh. DLS-2, Tab G at 2-3).

[26] The actual quantity of gas to be provided and the prices quoted are confidential information. Because of the confidential nature of this exhibit, the Department characterizes the gas prices in the January 28 Letter as the same as the gas commodity price in the project proposal.

and oil will be priced on a market sensitive basis, states what DLS and EME expect the gas commodity and transportation (on the Tennessee system) prices to be for 1994, and indicates the expected escalation rates for both commodity and transportation prices (id. at 3).

DLS contends that, in the February 13 Letter, EME restates "its agreement to provide 100% of the necessary fuel and transportation to the DLS project" (DLS Brief at 20). The February 13 Letter further describes EME's gas transportation arrangements, reiterates the gas commodity price expectations in the January 28 Letter, and cites even lower gas prices for February 1992 at a national trading center (Exh. DLS-10, at 2-3). The February 13 Letter concludes that the DLS bid's gas price escalation rate is "somewhat aggressive based on current market trends," noting a gas price decline or stability in most markets over the last four years (id. at 3).

Finally, DLS submitted the MidCon Letter to confirm the "market availability of fuel on the terms contained in the DLS proposal" (DLS Brief at 20, emphasis in original). The MidCon Letter identifies itself as "a letter of intent" (Exh. DLS-11). The MidCon Letter indicates that MidCon "can supply" gas daily to the DLS project, and specifies the 1995 starting price, annual price escalator, and length of contract period (id.).[27]

DLS also asserts that the fuel plan contained in the DLS bid assumes sufficient costs for gas transportation charges, referencing arrangements stated in the January 28 and

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[27] Because the information contained in the MidCon Letter is confidential, the Department characterizes the information as follows: the quantity of gas in the MidCon Letter is approximately one quarter of the amount in the January 28 Letter, the initial gas commodity price is modestly higher, and the escalation rate is higher (Exhs. DLS-2, Tab G, at 2; DLS-11).

February 13 Letters (DLS Brief at 18-19). DLS argues that gas transportation charges would not overlap but be proportionate, so that DLS would not pay charges on different systems at the same time for the same transported volumes (id. at 18-19). DLS claimed that, since the Tennessee Pipeline runs very near its site, little or no local transportation should be required (Exhs. DLS-1, at 10; DLS-4).

DLS contends that its fuel requirements would be met using firm and interruptible transportation arrangements, plus gas storage, by its fuel suppliers: EME and others such as MidCon (DLS Brief at 18). While DLS' bid assumed burning natural gas 100 percent of the time, DLS' Mr. Smith testified that he estimated that its facility might use No. 2 oil sometimes (Exh. DLS-1, Evaluation Sheets 1-5; Tr. 1, at 71). In a letter provided by DLS to BECo, EME stated that it has "window period" contracts on five pipelines, including two of the three pipelines EME plans to use to transport gas to the DLS facility, as well as firm transportation on the TransCanada Pipeline (Exh. DLS-10, at 2). EME also stated that it entered a long-term contract with the Transcontinental Gas Pipe Line ("Transcontinental") for winter storage service for the cogeneration market (id.).

DLS argues that BECo's claim that DLS incorrectly and inconsistently used LHV instead of HHV in its project proposal is unjustified, because: (1) the LHV is clearly marked and used consistently throughout the bid; (2) the LHV is an industry standard, used by the turbine manufacturers proposed in the bid; (3) the conversion from LHV to HHV is simple; and (4) the use of the LHV instead of HHV would only change the volume of gas consumed, but not the gas commodity price per MMBtu (DLS Brief at 23-24). DLS suggests that it does not matter whether it used LHV or HHV in its proposal, as long as

(1) DLS used the same heating value consistently throughout its proposal, or (2) the project remained viable when the heating value is properly adjusted (id.; DLS Response at 4).

3. Altresco

Altresco asserts that BECo's assessment that DLS significantly underestimated its gas commodity costs is accurate and reasonable (Altresco Brief at 18-19). To support its assertion, Altresco contends that: (1) the fuel supply agreement between EME and DLS is conditional,[28] and (2) the gas price projection contained in the DLS bid was far below (a) industry gas price forecasts, including the Department-approved forecast in RFP 3, and (b) market-clearing prices (id. at 18-19, citing Tr. 2, at 187-188, and Exhs. DLS-1, BE-2, at exh. C, and BE-4, at 2).

In arguing that DLS substantially understated its gas transportation costs, Altresco contends that DLS underestimated both long distance transportation costs and local distribution company ("LDC") charges (id., citing Exh. BE-4, at 2 and Tr. 2, at 187, 207-208). Altresco contends that DLS' transportation price assumption approximates the price for sending Canadian gas to Boston on the Tennessee system (id. at 19). Altresco contends that Canadian gas would require additional transportation on the TransCanada and Iroquois Pipeline systems to reach the Tennessee system, and that transportation on these pipeline systems would increase the total price of gas (id., citing Exh. BE-4, at 2). Altresco claims that transportation costs on this route would be several times the cost of sending Canadian gas to Boston on the Tennessee system (id.). Moreover, Altresco contends that

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[28] Altresco notes that EME did not indicate that it would be willing to guarantee the price it "expects" (id. at 23).

Tennessee's price for firm transportation of domestic gas from the U.S. Gulf Coast is far higher than the gas transportation price included in the DLS bid (id., citing Tr. 2, at 207). Altresco further argues that firm LDC transportation rates are well above what DLS included in its bid (id., citing Tr. 2, at 208).

Altresco contends that if DLS relies on EME's "window period" contracts for its fuel supply, DLS will be forced to burn more expensive oil for several months per year[29] (id. at 23, citing Exh. DLS-10 and Tr. 2, at 171-172, 178). Altresco points out that Mr. Reed stated that "window period" contracts refer to interruptible gas, that interruptible periods will not overlap significantly, and that gas can be interrupted for up to five months per year (id., citing Tr. 2 at 170-172, 177-178). Altresco asserts that lack of firm transportation is the biggest weakness in the DLS bid (id. at 24).

Altresco echoes BECo's assessment that DLS utilized an inappropriately low heat rate, thereby understating its facility's fuel use (or effective fuel price), and consequently its emissions, in turn raising the project's score (id. at 20). In particular, Altresco claims that the DLS bid was flawed by an inconsistency between an equipment heat rate expressed in LHV and a fuel supply expressed in HHV (id. at 20, n.13, citing Tr. 2, at 208-209).

D. Construction Costs

1. BECo

BECo claims that DLS failed to provide adequate documentation to support its cost

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[29] Altresco also suggests that oil use would also be associated with higher emissions than DLS claimed, which would harm DLS' price score (Altresco Brief at 20, 23; Exhs. DLS-5, at 3; DLS-14, exhibit F at 1).

allowance for engineering, procurement, and construction (BECo Brief at 14). BECo claimed that DLS' construction cost estimates were too low, about 20 percent lower than those for BECo's Edgar unit (a comparable 306 MW gas-fired combined cycle plant), and significantly lower than those of RFP 3 competitors (BECo Memorandum at 14). BECo maintained that the total price proposed by DLS was less than the capital recovery portion of the projected price for two other comparable RFP 3 projects (Exh. BE-1, at 9). BECo also claims that the quotes for construction and engineering costs submitted by DLS in the months after its bid (1) were based on different project specifications than those proposed by DLS, and (2) did not indicate which pieces of equipment were included in the quotes (BECo Brief at 14). According to BECo, in the absence of reliable supporting documentation from DLS, BECo relied on its own expertise and the experience of RCG to conclude that DLS' construction cost assumptions were unrealistic (id.).

2. DLS

DLS argues that BECo's contentions that DLS' projected construction costs were 20 percent below those of BECo's own Edgar project, and substantially below those of other RFP 3 proposals, represent improper comparisons (DLS Brief at 21). DLS contends that

> [u]nless the comparison is made to a similarly financed non-cogeneration facility [note omitted] (not a utility sponsored plant which may require (a) union labor to build and operate, (b) additional capital costs, or (c) financing not comparable) of the same size as DLS, any comparison is fundamentally flawed and not an accurate reflection of market conditions.

(id.). DLS claims that, since larger plants can achieve "economies of scale," BECo's comparison of the DLS plant to smaller plants on a per kilowatt basis is not meaningful (id.).

DLS asserts that Kendall Capital Partners, L.P. ("Kendall") [30] sent BECo a letter with a second, revised pro forma[31] on April 9, 1992, which DLS claims supported the construction cost allowance contained in the DLS bid (id.; Exh. DLS-5).

To support its position that the construction cost allowance in its initial pro forma was realistic, DLS submitted four one-page construction cost quotes for combined cycle plants, which had been submitted to BECo during the RFP 3 Review Period, from various suppliers including Westinghouse and General Electric (DLS Brief at 21-22, referring to Exhs. DLS-6 through DLS-9).[32] Relying in part on these four quotes, DLS contends that the construction cost allowance in its proposal is "certainly within the market range" (DLS Brief at 21). DLS states that BECo never asked to see additional quotes nor inquired about the terms of the quotes provided (id. at 22).

3. Altresco

Altresco asserts that BECo's assessment that DLS significantly underestimated its construction costs was accurate and reasonable (Altresco Brief at 16-18). Altresco gives five

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30 DLS claims that Kendall has raised $4 billion for IPPs in the last two years (Exh. DLS-1, Document 4, at 1). DLS also claims that Kendall is unaffiliated with DLS (DLS Brief at 21).

31 A pro forma is a document that contains a budget and various financial statements. RFP 3 requires a bidder to develop and submit a pro forma (§ 3.7.6). DLS submitted its initial pro forma on January 31, 1992 with its project proposal (Exh. DLS-1, Document 4, at 2-7).

32 Because the information contained in the four quotes is confidential, the Department characterizes the information as follows: one quote was for a plant of unspecified size for less than DLS' cost allowance (Exh. DLS-6); another quote was for a plant about the same size as DLS proposed, at the same per kilowatt cost assumed in the DLS proposal (Exh. DLS-7); the two other quotes were at somewhat higher prices per kilowatt for plants smaller than DLS proposed (Exhs. DLS-8; DLS-9).

reasons for its assertion: (1) BECo and RCG used a data base (developed in part by RCG in its work for many NUGs) which included most of the major developers in the country, as well as the vendors, engineers, and consultants used by DLS; (2) most projects in the data base use technology similar to DLS'; (3) a cogenerator is likely to have lower construction costs than an IPP, not higher costs; (4) there are likely only minor economy of scale differences between a 200 MW and a 300 MW combined cycle unit; and (5) there is no basis in the record for the DLS claim that its project will obtain vendor financing[33] (id. at 16-17). Altresco further maintains that: (1) none of the plant cost quotes submitted by DLS (Exhs. DLS-6 through DLS-9) are for the equipment identified in the DLS proposal; (2) it is not clear that any of the plant cost quotes include all necessary equipment and engineering services; (3) the plant cost quotes are not firm price offers; and (4) the price in two of the plant cost quotes exceeds the construction cost in DLS' initial pro forma, contained in the DLS proposal (id. at 22).

E. Financing

1. BECo

BECo claimed that DLS' interest during construction ("IDC") cost allowance was too low and out of line with market expectations (BECo Memorandum at 12, 15). In particular, BECo compared the IDC allowance for the DLS proposal against two other comparable, but

[33] In one type of vendor financing, an equipment manufacturer provides the equipment in exchange for an ownership interest in the plant where the equipment is installed.

smaller, proposals in RFP 3 (id. at 15).[34] BECo added that no lender attested to the existence of a hypothetical "better-than-market" deal (id.).

2. DLS

DLS argues that BECo's claim that DLS' IDC allowance provides insufficient contingencies for cost-overruns shows BECo's lack of understanding of the project's system of vendor financing,[35] and is an improper basis for disqualification (DLS Brief at 22). DLS claims that its proposal was based on vendor financing (id.). DLS' Mr. Smith explained that, if DLS could obtain vendor financing, the costs of the equipment supplied by the vendor would not be subject to interest charges to DLS, and thus DLS would pay interest on only a small fraction of its overall construction costs (Tr. 1, at 114-115).

DLS asserts that any financial risk in the project is borne by DLS, and that the project has sufficient debt coverage and profit margin to cover any economic risk, such as cost overruns (id. at 22-23). DLS further claims that its contingency allowance, greatly augmented (from its submitted proposal) for demonstration purposes in its second pro forma (Exh. DLS-5), was adequate to cover extra IDC and other contingencies, while keeping the project highly financeable in terms of debt-service coverage and return on equity (DLS Brief

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34 Because of the confidential nature of the information, the Department characterizes the IDC amounts cited by BECo as approximately four and six times as high as DLS' IDC allowance.

35 DLS' Mr. Smith stated that he hoped to obtain vendor financing for certain capital equipment (Tr. 1, at 114). DLS stated in its proposal that it planned to finance its proposal by a 20-year single investor lease, citing past lease proposals from General Electric Capital Corporation, "the premier institutional investor in the power business today" (Exh. DLS-1, Document 4, at 1).

at 22-23; Tr. 1, at 114-117). DLS provided its second pro forma to BECo during the RFP 3 Review Period to illustrate the viability of DLS' proposed project using even unfavorable assumptions (DLS Brief at 22).[36] DLS asserts that BECo's Review Team and RCG should have known that the DLS proposal contained a substantial margin to support financing issues raised by BECo (id. at 23).

3. Altresco

Altresco raises questions about the nature of DLS financing and its debt coverage[37] (Altresco Brief at 17-18, 21-22). Altresco claims that DLS' IDC allowance is unrealistically low (id. at 17-18). Altresco notes that DLS plans to use IDC only for developer fees, which are very small compared to the costs associated with actual capital equipment (id. at 17, citing Tr. 1, at 114). Altresco argues that there is no basis in the record to conclude that DLS will obtain vendor financing, which would be required to justify the fact that DLS made no specific allowance for IDC costs for equipment (id. at 17). Altresco contends that, with vendor financing, the vendor would indeed pay interest during construction, but the vendor would then collect those interest costs back from DLS in the form of higher capital charges

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36 Because of the confidential nature of the information, the Department characterizes the second pro forma as follows: compared to the pro forma in the DLS proposal, the second pro forma increases the contingency allowance, debt service reserve, and proportion of debt in the overall capital structure, decreases the net present value (profit) and debt coverage ratios, and leaves the internal rate of return no longer applicable (Exhs. DLS-5, at 3; DLS-1, Document 4, at 2-3). DLS asserts that, even in the above scenario, the project would be financially viable (DLS Brief at 22).

37 Debt coverage is measured by a debt coverage ratio, which is the ratio of a year's operating income (revenue less ordinary expenses) to that year's required debt payment. A high debt coverage ratio raises the confidence of potential investors that a company will be able to pay its debts.

(id. at 18).

Altresco further asserts "that there is no assurance that the DLS project could achieve 100 percent debt financing" (id. at 21, citing Tr. 2, at 150). Altresco also observes that "Exhibit DLS-5 shows a minimum debt coverage ratio for total debt of only 1.00. [DLS] testified that if the debt coverage ratio fell below 1.00, there would be a default" (id. at 22, n.14, citing Tr. 1, at 75-76).

F. Overall Price

1. BECo

BECo stated that "the fixed, guaranteed price presented in the [DLS] proposal is based on erroneous, uncertain, or questionable assumptions" (BECo Brief at 8, citing Exh. BE-1, at 10). In its May 19, 1992 letter disqualifying DLS' proposal, BECo stated that the price stream in its bid represented less than half to BECo's avoided costs and was "not consistent with the Company's experiences in pricing for similar projects which have been designed based on prudent engineering practice" (Exh. DLS-2, Tab A). BECo claims that, based on a comparison of the DLS proposal to other RFP 3 project proposals and the winner of BECo's RFP 2, DLS' price bid was completely inconsistent with the market (BECo Brief at 8, citing Exhs. BE-1, at 8-9, and BE-2, at 3). BECo contends that price comparisons to other proposals are appropriate for evaluating proposals, because a solicitation process is designed to allow a utility to compare all currently available supply resource options (id. at 11). Finally, BECo stated, "[t]aken together, the various understatements and overly optimistic assumptions of key elements of the bid had the cumulative effect of so understating the overall cost of the project as to render the entire bid unviable and unrealistic" (id. at 9).

Mr. Killgoar summed up BECo's evaluation by answering that, even considering all the information submitted by DLS after its initial proposal to BECo, his decision to disqualify the DLS project would have been the same (id. at 12, citing Tr. 2, at 205-206).

2. DLS

DLS indicates that on May 20, 1992, BECo requested the Department to defer further activities in RFP 3, citing revised avoided cost estimates which were 40 percent lower than the original ceiling prices of RFP 3 (DLS Brief at 13). DLS disagrees with BECo's determination that DLS' bid price was too low because it was less than half of BECo's original ceiling price (id. at 10, 13-14). DLS argues that the DLS bid would be the only proposal to offer power at a price substantially below BECo's revised avoided cost, and thus in keeping with a utility's fundamental obligation to provide its customers with a least-cost reliable power supply (id. at 13). In summarizing the benefits of its project, DLS quotes BECo's witness, Mr. Killgoar: "[i]f in fact the [DLS] project could be developed and deliver power at those rates, it would be a good project" (id. at 28, citing Tr. 2, at 168).

3. Altresco

Altresco contends that BECo had at least four separate bases for its decision, that any of the four would have been a reasonable basis for disqualification, and that "[c]umulatively, the four provide overwhelming justification for BECo's actions" (Altresco Brief at 14). The four bases consist of: (1) DLS' overall price bid, compared to other bids and BECo's ceiling prices; (2) DLS' understated construction costs, including IDC; (3) DLS' "enormous" understatement of gas commodity and transportation prices; and (4) DLS' implausibly low heat rate (id. at 15) Altresco asserts that BECo's assessment that the DLS bid price was

unrealistically low, compared to other RFP 3 project proposals and a generic 300 MW facility, is accurate and reasonable, because (1) it is difficult for any one project developer to gain such a large price advantage in a competitive market, and (2) most bidders are using the same gas-fired combined cycle generation technology as DLS (id. at 16).

Altresco agrees with BECo that, even if BECo had considered all of the supplemental information submitted by DLS, BECo's decision to disqualify the bid would not change and would still be reasonable (id. at 21, citing Tr. 2, at 206). Altresco argues that this is especially true since most of the supplemental information submitted by DLS provided no further guarantee of its fuel plan, and raised new issues concerning gas supply interruptions and the consequent need to provide for oil costs in the bid (id. at 23).

G. Application of the RFP 3 Provisions

1. BECo

BECo asserts that the DLS price bid was outside the "range of reasonableness" (BECo Brief at 8-9). BECo maintains that because the DLS price bid was not reasonable, the project's price factor score was too high, which overcompensated for minimal project viability and confidence scores (id.). BECo argues that it could not rely on the RFP scoring system alone, because the scoring system does not adequately account for the high risk associated with the DLS project (id.). BECo stated that if DLS had bid a price "within the range of reasonableness, the risk associated with project viability would have been sufficiently accounted for in the scoring system" (id.). BECo contends that "there are ways, no matter how much you try to guard against them, where unrealistic projects can find themselves into the award group" (id. at 9, citing Tr. 2, at 179). BECo regarded Section

3.8.1(n) of RFP 3 as a safety valve to address this situation (Tr. 2, at 181). Therefore, BECo argues that it invoked RFP 3 Section 3.8.1(n) to disqualify DLS, because DLS could not offer reliable power pursuant to the terms and conditions of its proposal (id. at 7).

BECo avers that the purpose of the RFP process is to select projects for the RFP 3 Award Group which "best balance value to BECo's customers with Project viability and BECo's needs" (BECo Brief at 9, citing Exh. DLS-14, at 19). BECo also argues that the RFP 3 process developed by BECo was "exceptionally thorough, reliable and well thought out," and was based on experience gained in RFPs 1 and 2 (id. at 1). BECo asserts that it had no motivation to subvert the purpose of RFP 3 (to acquire least-cost reliable power) and designed RFP 3 and its project proposal review process to accomplish this purpose (id. at 1-3). BECo argues that in an increasingly competitive environment, it has great incentive to select the best bid in order to maintain its competitive position (id. at 2). If its decision to disqualify DLS' proposal is overturned by the Department, BECo argues that the integrity of the bidding process and its ability to avoid contracting with non-viable projects would be jeopardized (id. at 1-2).

BECo stated that it based its disqualification decision on a series of factors and the overall bid (id. at 13). BECo contends that it disqualified the DLS project proposal because it was unrealistic and the proposed project was not viable, rather than because of any single error, omission, or misrepresentation in the DLS proposal (id. at 8). BECo emphasizes that its evaluation and disqualification decisions were "consistent with [BECo's] obligations under RFP 3" (id. at 9).

In applying the appropriate standard of review, BECo concludes that DLS failed to

meet its burden to prove that BECo had no reasonable basis for its disqualification decision (id. at 6). BECo argues that, given what it knew or should have known, its disqualification decision was based on careful consideration of the DLS proposal, in accordance with the provisions of RFP 3, as well as comparison to other similar projects, and was therefore reasonable (id. at 3, 14-15).

2. DLS

DLS argues that BECo's avoided cost comparison and BECo's doubt concerning the viability of the bid are inappropriate as a rationale for the disqualification of its proposal, because the RFP 3 scoring provisions were specifically designed to assess the likelihood of project success (DLS Brief at 14-15). DLS cites the price, economic confidence, project development confidence, operational longevity confidence and system optimization ranking criteria factors of RFP 3 (§§ 5.1 et seq.) to illustrate how the scoring system is specifically designed to weigh tangible and intangible factors of a project proposal which would indicate a project's likelihood of success (id. at 8-9). DLS argues that these ranking criteria factors were designed to optimize benefits, while reflecting the risks that project proposals would impose on ratepayers (id.).

DLS claims that its proposal was the only one to offer power at a price substantially below BECo's revised avoided cost, and thus disqualification of the DLS proposal would be inconsistent with a utility's fundamental obligation to provide its customers with a least-cost reliable power supply (id. at 13). DLS asserts that BECo's decision to disqualify the DLS bid would irreparably harm DLS and the integrity of the RFP process (id. at 1). DLS also contends that BECo's ratepayers would pay more than they should and more than BECo's

revised ceiling price, in violation of PURPA,[38] Department regulations, and the terms of RFP 3 (id. at 28).

In applying the appropriate standard of review, DLS contends that BECo's disqualification of its proposal was unreasonable, based on what BECo knew or should have known about the DLS proposal at the time of its disqualification (id. at 10). DLS asks that the Department "not concur in the purported disqualification of the DLS proposal" (id. at 1).

3. Altresco

Altresco claims that BECo applied provisions of RFP 3 consistently and in accord with their stated purpose (Altresco Brief at 2, 8). Altresco asserts that Section 3.8.1(n) worked exactly as planned to protect the integrity of the RFP process (id. at 13, n.7). Altresco contends that DLS' project proposal failed to constitute a bona fide bid, and that "in order to be an eligible proposal, it must be a bona fide one. The ranking formula will work so long as all the bids are realistic, good faith ones" (id.). Altresco argues that a project proponent could always "gain the highest score by bidding an unrealistically low price. No combination of non-price points can prevent this" (id.). Altresco claims that a requirement like Section 3.8.1(n) is the only way to avoid such abuse of the RFP process (id.).

Altresco states that "[f]or BECo to have done anything other than to disqualify DLS would have been unfair to all other bidders and would have threatened the integrity of the entire RFP process" (id. at 13). Altresco also argues that to grant DLS' requested relief would subvert the RFP process by forcing BECo to score a non-viable project proposal and

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[38] Public Utility Regulatory Policies Act of 1978, Pub.L. No. 95-617, as amended.

possibly include it in the Award Group (id. at 24-25). Finally, Altresco notes that the purpose of PURPA is to foster development of a competitive market in the power-generation industry, which requires "responsible and competent practitioners to actually bring into service non-utility generation," and that allowing "low-ball" bidders to obtain power contracts would contravene this goal (id.).

In applying the appropriate standard of review, Altresco asserts that the DLS case is far from a close call (id. at 13). Moreover, Altresco argues that BECo gave DLS the benefit of the doubt in two disqualification situations (id., n.8).[39] Altresco asserts that BECo's decision to disqualify the DLS proposal was reasonable and in accord with Department precedent and the terms of RFP 3, based on what BECo knew or should have known about the bid (id. at 3, 25-26).

IV. ANALYSIS AND FINDINGS

A. Standard of Review

In reviewing BECo's actions in disqualifying the DLS project proposal, the Department employs a standard of reasonableness. The Department will not grant DLS' petition unless DLS proves that BECo's disqualification of the DLS proposal was unreasonable.

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[39] In making this argument, Altresco refers to Sections 3.7.5 and 3.7.7 of RFP 3 (Altresco Brief at 13, n.8). Section 3.7.5 requires detailed project-specific cost breakdowns for estimated capital expenses and operation and maintenance expenses. Section 3.7.7 requires satisfactory evidence of market access to, or availability of, the primary and secondary fuels for the contract term. Altresco contends that since DLS included some supporting information on fuel access and capital costs, BECo construed these two threshold requirements liberally (id.).

DLS, citing MASSPOWER, urges the Department to narrow the reasonableness standard and approve the disqualification only if the DLS proposal is not cost-effective. DLS misconstrues MASSPOWER and the goal of the RFP process. MASSPOWER did not hold that a project proposal may be disqualified only if it is not cost-effective, but rather that cost-effective bids may not be summarily disqualified for deficiencies that are mere technicalities. MASSPOWER at 30, 35.

DLS also urges the Department to consider the harm to DLS and to ratepayers which may result from disqualification of DLS' low-priced bid. The overriding goal of the RFP process is to maximize net benefits to ratepayers. 220 C.M.R. § 8.05(c). As the Department-approved RFP 3 scoring system shows, cost-effectiveness is only one factor to be considered, and must be balanced with reliability and project viability when assessing whether a project proposal will provide benefits to ratepayers. In addition, harm to the competitive bidding process from selection of unrealistic projects must be considered, because of its potential long run effects on the development of a competitive generation market that will provide least-cost resources for ratepayers.

On the other hand, BECo asserts that company judgments should be presumed reasonable and should not be overturned unless a company is so unreasonable and so arbitrary that no reasonable justification for company actions is possible. The Department reaffirms its position that an electric company must be allowed a measure of discretion in managing the RFP process, but that discretion is not unlimited and must be subject to meaningful Department review. See Destec at 13-14. The wide reading of the reasonableness standard urged by BECo would make it nearly impossible for an aggrieved

bidder to prevail in any disqualification dispute. The integrity and fairness of the RFP process would suffer if bidders were effectively denied any appeal of allegedly improper disqualification decisions.

Therefore, the Department finds that it would be inappropriate either to narrow or to expand the reasonableness standard in this proceeding. The Department thus evaluates whether BECo's assertion that DLS would not be able to fulfill the terms and conditions of its proposal in violation of Section 3.8.1(n) of RFP 3 is in accord with Department precedent and policy, which states that a bidder should not be disqualified if its failure to conform to a provision of an RFP is a mere technicality. Specifically, the Department will examine not only whether any deficiencies in the DLS proposal are contrary to RFP provisions, but also whether those deficiencies are significant enough to warrant BECo's conclusion that the DLS project proposal should be disqualified. The Department will assess BECo's actions as a whole, since the disqualification decision was based on a cumulation of many factors. Finally, the burden is on DLS to prove that BECo's disqualification decision was unreasonable in light of what BECo knew or should have known during the RFP 3 Review Period.[40]

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[40] We think that it is inappropriate to remove the burden of proof or burden of production of evidence from the disqualified bidder in future IRM disqualification disputes. The most likely effect of such a shift would be to afford an opportunity to, and thereby encourage, marginally qualified or unqualified bidders to pursue their goals administratively rather than in the marketplace. In this case we have reaffirmed the current reasonableness standard and placement of the burdens of proof and production that were sufficient to allow the Department to overturn inappropriate disqualifications in MASSPOWER and Wheelabrator. Therefore, consistent with our determination to place the responsibility of administering competitive solicitations on

(continued…)

B. BECo's Review Process

Consistent with the Department's decision to grant a measure of discretion to the companies in managing their RFP processes, it is generally within BECo's discretion to determine which company representatives and outside consultants will review project proposals, and how much time will be devoted to that review. For RFP 3, BECo augmented its own expertise, gained by developing and administering two previous RFPs and planning a new unit at Edgar station, by hiring RCG, a consultant with experience in numerous competitive solicitations. BECo and RCG also had the benefit of comparing the DLS proposal with the 40 other bids submitted in RFP 3. DLS has failed to persuade the Department that BECo did not establish a review process consistent with its RFP objectives.

The provisions in RFP 3 clearly state that it is the bidder's responsibility to provide documentation adequate to allow BECo to verify the assertions in the project proposal (§ 4.3.6(b)). In reviewing the documentation provided with the DLS bid, the Department agrees with BECo that the documentation was inadequate in many areas (see Sections IV.C-IV.F, below).[41]

DLS claims that BECo did not follow its own procedures, by not seeking clarification of the DLS bid or using DLS' supplemental information to determine whether to disqualify

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[40](…continued)
the utility, we find that it best serves the public interest to leave the burdens of proof and production on the petitioner in future disqualification disputes.

[41] Even if the Department considers the documentation provided after the bid due date and during the RFP 3 Review Period, DLS' documentation still fails to establish key components of DLS' proposal (see discussion in Sections IV.C-IV.F, below).

DLS. BECo and Altresco claim that, according to Section 4.3.6, seeking clarification would have violated the terms of RFP 3 unless the DLS bid was ambiguous. DLS did not assert that the RFP or its bid were ambiguous. The Department finds that BECo reasonably concluded that the documentation provided by DLS generally was not ambiguous, but rather it was insufficient to support the prices and assertions included in the bid[42] (see Sections IV.C-IV.F, below). In addition, BECo's interpretation of Section 4.3.4 of RFP 3 to preclude accepting additional documentation, absent ambiguity, is reasonable. Therefore, the Department finds that DLS has not shown that BECo failed to follow its own procedures or comply with the relevant information requirements of RFP 3 with respect to the DLS proposal, or that BECo applied its RFP 3 review process to the DLS proposal in a discriminatory, inadequate, or inconsistent manner.

C. Fuel Costs

BECo and Altresco dispute DLS' claim that it had a binding agreement for all its fuel needs. BECo and Altresco also argue that the DLS gas price assumptions were unrealistically low and inconsistent with the market, while DLS contends that its gas price assumptions were realistic and consistent with market conditions during the RFP 3 Review Period.

The documentation provided by DLS to support its gas supply assertions is vague in several aspects. The January 28 Letter states that EME will sell fuel priced "on a market

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[42] For example, a reasonable reading of the words in Mr. Gray's notes dated February 11, 1992, "looking for more documentation re: fuel arrangements," which DLS relied on, is that DLS' documentation was insufficient.

sensitive basis," together with what DLS and EME "expect" the relevant prices to be. The January 28 Letter cites expectations but fails to firmly establish several key points, notably the gas commodity prices, the transportation routes, and the gas commodity and transportation price escalation rates. Because the January 28 Letter is expressly conditioned on the parties "entering into a specific contract embodying these terms and conditions by December 31, 1992,"[43] the Department does not consider it to be a binding agreement between DLS and EME.

The February 13 Letter reiterates the gas commodity price expectations contained in the January 28 Letter, cites even lower gas prices for February 1992 at a national trading center, and asserts gas price decline or stability over the last four years. Therefore, the February 13 Letter from EME does no more than the January 28 Letter to commit to gas commodity prices or escalation rates.

The MidCon Letter states "[p]lease consider this a letter of intent" that MidCon "can supply" about a quarter of the DLS fuel requirement, starting at a price modestly higher than that expected in the January 28 Letter. The MidCon Letter characterizes itself as a "letter of intent of [MidCon] to enter into negotiations," and is also expressly conditioned on "satisfactory negotiations of all necessary agreements."

In view of the lack of commitment to a firm agreement expressed in the first three documents provided by DLS to support its fuel arrangements, and the fact that the MidCon letter of intent covers only about a quarter of the necessary fuel, the Department cannot find

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[43] There is no evidence in the record that DLS entered into such a contract by December 31, 1992.

that BECo was unreasonable in concluding that DLS failed to secure binding agreements for its fuel arrangements.

Because the documentation submitted with the DLS proposal did not establish firm commitments for fuel arrangements, it was reasonable for BECo to consider general market prices in assessing whether DLS' fuel price assumptions were realistic.[44] The market information available to the Department, BECo and developers about gas prices during the entire RFP 3 Review Period (roughly the first five months of 1992) indicates that gas commodity prices were exceptionally low in February 1992, but rose sharply during the rest of the RFP 3 Review Period. Thus, in early 1992 DLS might have been able to secure its gas supply at prices similar to those in its proposal. However, DLS did not secure contracts locking in the favorable prices of February 1992, and offered a letter of intent for only about a quarter of its needs at prices modestly above February 1992 levels. Accordingly, the Department finds that DLS once might have been able to secure enough gas for its facility at prices roughly as low as those in its proposal, but that it did not do so while it could.

The parties have argued about the realism of the assumed gas transportation prices in the DLS proposal. The Department recognizes that DLS may acquire gas via more than one route, so that the average transportation price would be proportionate to the amounts and the

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[44] The Department notes that Exhibits DLS-4, DLS-10, and DLS-11 were filed weeks after the bid deadline and not with the DLS bid as supporting documentation. They are considered above only to help the Department determine what BECo knew or should have known during the RFP 3 Review Period (Hearing Officer Ruling, August 12, 1993).

prices over the various routes.[45] However, based on BECo's and Altresco's claims about long-distance rates for firm and interruptible transportation of domestic and Canadian gas over various routes, the Department finds it likely that DLS' actual average transportation price would exceed the average transportation price allowance in DLS' proposal by a factor of two or more.[46] In addition, the Department is concerned that LDC charges will be substantially higher than the zero charge that DLS assumed, since the Tennessee Pipeline runs only near, but not across, the DLS site, suggesting that DLS will have to pay LDC charges.

Altresco has raised concerns, based on documents submitted by DLS from the RFP 3 Review Period, that the DLS gas supply is interruptible. Altresco cites testimony by a BECo witness, Mr. Reed, that "window period" contracts cited in Exhibit DLS-10 refer to interruptible gas transportation. The "window period" and winter storage information may

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45 Gas comes to Massachusetts primarily from two areas, the U.S. Gulf Coast and Alberta in western Canada. Gas from Alberta travels 2000 miles across Canada in the main TransCanada Pipeline to a junction 200 miles north of Toronto. From there it travels (1) south around Lake Ontario, using the TransCanada Pipeline system to Niagara Falls and then the Tennessee Pipeline to the Boston area, or (2) north around Lake Ontario on the TransCanada system to the St. Lawrence River, then through an Iroquois Pipeline to join the Tennessee Pipeline outside Albany, finishing its journey to Boston on the Tennessee Pipeline. Gas from the Gulf Coast travels 2000 miles (1) in the main Tennessee Pipeline directly from the Gulf Coast to the Boston area, or (2) in any of several other pipelines to the Northeast, where it uses the Algonquin or Tennessee Pipelines to reach Boston.

46 The Department notes that Exhibits DLS-10 and DLS-11 were not included with the DLS bid as supporting documentation. They are considered above only to help the Department determine what BECo knew or should have known during the RFP 3 Review Period (Hearing Officer Ruling, August 12, 1993).

be firm-specific information which BECo should not have been expected to know.[47] Even if BECo were to suppose that DLS had access to such arrangements, it appears that DLS' gas supply was largely interruptible.[48] The low transportation price which DLS quoted in its bid further suggests that much of its gas supply is interruptible. The Department notes that no documentation in the DLS proposal supports the DLS assumption that it will have firm gas supplies. Therefore, a substantial portion, if not all, of DLS' gas supply is likely to be interruptible. With an interruptible gas supply, DLS would likely burn significant amounts of oil, which would increase the DLS project's emissions[49] and thus lower its overall price score. Similarly, due to the interruptibility factor, DLS likely has significantly underestimated its fuel costs. Alternatively, DLS likely has significantly underestimated its cost of obtaining firm gas transportation year round.

The parties agree that natural gas is sold on an HHV basis but that DLS stated its plant's heat rate on a LHV basis. The effect of using LHV instead of HHV for plant heat

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47 The Department again notes that Exhibit DLS-10 was not included with the DLS bid as supporting documentation. It is considered above only to help the Department determine what BECo knew or should have known during the RFP 3 Review Period (Hearing Officer Ruling, August 12, 1993).

48 The Transcontinental Pipeline runs from Texas to New Jersey. Winter storage on Transcontinental may ameliorate interruption somewhat, but gas stored in winter even in New Jersey (the northern end of the pipeline) would still require firm transportation to the DLS facility in Massachusetts, in order to supply 100 percent of DLS' fuel needs, as shown in the DLS proposal.

49 The proposed plant's planned heat rate is 59 percent higher for oil use than for gas, so that more fuel must be burned to produce the same amount of electricity (Department characterization of confidential data in Exhibit DLS-5, at 3). In addition, for the same heat content, burning oil instead of gas produces substantially more of several pollutants (Department characterization of confidential data in Exhibit DLS-5, at 3; RFP 3, exhibit F at 1).

rate, while using HHV for gas prices, is that DLS would require eleven percent more gas by volume than assumed in the DLS proposal, as DLS argued. Although adjusting for this difference is a simple calculation, DLS would be required to buy eleven percent more gas, so gas purchase expenses will be eleven percent[50] greater than assumed in the DLS bid. Therefore, the Department finds that DLS, due to the heating value factor alone, has underestimated both its fuel costs and its emissions by approximately eleven percent.

Accordingly, given the problems identified above with the gas commodity cost, local and long-distance gas transportation costs, interruptibility, and heating value, and in light of what BECo knew or should have known regarding fuel costs during the RFP 3 Review Period, the Department finds that DLS has failed to establish that BECo was unreasonable in concluding that the overall fuel supply costs assumed by DLS are unrealistic and substantially understated.

D. Construction Costs

BECo and Altresco have argued that the DLS construction cost allowance is unrealistically low, while DLS contends that its construction cost allowance is realistic and consistent with market conditions during the RFP 3 Review Period. The Department notes that the DLS construction cost allowance was not supported in its proposal by any contract, letter of intent, letter of interest, or other documentation sufficient to establish that the construction cost allowance was realistic. DLS later provided only one construction cost

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[50] The actual number will be smaller to the extent that No. 2 oil, the backup fuel, is burned during gas interruptions. The HHV to LHV ratio for No. 2 oil is about 1.06.

quote which clearly supports[51] DLS' bid pro forma construction cost: the same cost per kilowatt for a plant approximately the same size (Exh. DLS-7). However, not even this quote specifies whether all the necessary equipment in the DLS project proposal is included. Assuming that the projections in Exhibits DLS-6 through DLS-9[52] include all necessary equipment and represent relevant information about market conditions during the RFP 3 Review Period, it is unlikely, but possible under favorable conditions such as sluggish demand for equipment, that DLS could build the plant for the construction cost allowance in its bid pro forma.[53]

However, DLS failed to document that it could achieve its projected construction costs, both when submitting its bid and subsequently, pursuant to Sections 3.7.5 and 4.3.6 of RFP 3. Accordingly, the Department finds that, in light of what BECo knew or should have known regarding construction costs during the RFP 3 Review Period, DLS has failed to establish that BECo was unreasonable in concluding that the DLS construction cost allowance was too low.

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51 One quote did not specify the plant size, while the two other quotes had higher prices per kilowatt than DLS' proposal.

52 The Department again notes that Exhibits DLS-6 through DLS-9 were not included with the DLS bid as supporting documentation. They are considered above only to help the Department determine what BECo knew or should have known during the RFP 3 Review Period (Hearing Officer Ruling, August 12, 1993).

53 However, given that DLS' bid is 306 MW and DLS has expressed an intention to reduce its plant size to 130 MW (Exh. BE-5), conditions may need to be even more favorable for DLS to successfully complete construction of the plant for the assumed price, since DLS might thus lose most of the scale economies it claims.

E. Financing

BECo and Altresco contend that DLS' IDC cost allowance is too low or unrealistic, while DLS contends that this IDC charge is realistic in light of DLS' financing plan. Altresco claims that DLS failed to provide supporting documentation for vendor financing with its bid. Assuming that DLS could obtain vendor financing, IDC charges might be included in capital costs, thereby increasing capital costs, and causing vendor financing costs to significantly exceed the IDC allowance provided in the DLS bid pro forma. Therefore, the Department finds it likely that DLS has underestimated its IDC costs. Accordingly, the Department finds that, in light of what BECo knew or should have known regarding IDC costs, DLS has failed to establish that BECo was unreasonable in concluding that DLS' IDC cost allowance was too low.

Altresco has called attention to possible problems with debt financing and debt coverage, based on the DLS pro formas. The DLS proposal appears internally inconsistent with respect to the amount of equity in the project (Exh. DLS-1, Document 4, at 1-3). Furthermore, DLS' second pro forma is inconsistent with the initial proposal (Exh. DLS-5, at 3). The record is unclear regarding the type of financing DLS proposes.

Absent the many problems noted above with fuel and construction cost assumptions, significant equity financing may leave satisfactory debt coverage ratios. However, if the project were to be 100 percent debt financed, the project would depend on its debt reserve to avoid default on its debt.[54] Because DLS has underestimated its fuel costs and probably its

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[54] The minimum total debt coverage shown in the revised pro forma (Exh. DLS-5), when DLS' planned debt reserve fund is added, is significantly higher than 1.00.

(continued…)

construction costs, DLS' debt coverage ratio might fall far below that shown in the DLS pro formas, perhaps well under 1.00, even to the point of exhausting the debt reserve. As Altresco noted, DLS' witness admitted that if the debt coverage ratio fell below 1.00, that would constitute default. The Department is concerned that DLS would use a substantially higher percentage of debt financing than DLS identified in part of its first pro forma, jeopardizing its (1) its ability to support debt payments, and (2) its ability to finance the project.[55] Once again, DLS has failed to provide adequate documentation of or to justify key cost factors in its proposal.

F. Overall Price

BECo and Altresco assert that the overall DLS price is based on numerous erroneous or questionable assumptions. DLS notes that its proposal is the only bid to offer energy at a price substantially below BECo's revised avoided cost, which demonstrates that it is the least-cost bid. The Department has found serious problems with the assumptions underlying DLS' price bid in Sections IV.C-IV.E above. Specifically, the Department has found that: (1) DLS has a letter of intent for only about a quarter of its fuel requirements, and no longer can obtain fuel contracts at prices nearly as advantageous as those in its proposal; (2) DLS'

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[54](…continued)
However, DLS anticipates that its debt reserve would not be funded from revenues during the first year of the project's operation; instead DLS plans to fund the reserve up front, as part of the project's capital cost (Exhs. DLS-1, Document 4, at 2; DLS-5, at 3; Tr. 1, at 75).

[55] The Department notes that Exhibit DLS-5 was not included with the DLS bid as supporting documentation. It is considered above only to help the Department determine what BECo knew or should have known during the RFP 3 Review Period (Hearing Officer Ruling, August 12, 1993).

actual transportation price likely would exceed the transportation price in its proposal by a factor of two or more; (3) DLS probably significantly underestimated its project's fuel costs and emissions, because either oil would be required for a substantial part of the year, or higher costs would be incurred for firm natural gas; (4) DLS erred in its heat value calculations, understating its fuel costs and its emissions by eleven percent; (5) DLS failed to substantiate that it could achieve its low construction cost projection; (6) DLS probably significantly underestimated its interest cost during construction; and (7) DLS failed to document or even explain the exact nature of its financing, raising concerns about the financeability of the DLS project. While none of these problems alone may have rendered the overall DLS bid price unrealistic,[56] the cumulative deficiencies are very substantial and a more than sufficient basis for BECo to conclude that the DLS price proposal was unrealistically low. Accordingly, the Department finds that, in light of what BECo knew or should have known at the time, DLS has failed to establish that BECo was unreasonable in concluding that the overall price was unrealistically low and based on erroneous or questionable assumptions.

G. Application of the RFP 3 Provisions

DLS asks the Department to declare its proposal the winner of RFP 3, because: (1) it is the only proposal to offer power at a price substantially below BECo's revised

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[56] For example, if use of the wrong heating value were the only problem with the DLS proposal, the proposal might not merit disqualification. See MASSPOWER at 14-18, 34-35. BECo could perform a simple calculation to convert LHV to HHV, adjust DLS' price score based on the project's revised projected emissions, and then examine whether fuel costs eleven percent higher than DLS assumed would result in DLS being unable to fulfill the terms and condition of its proposal.

avoided costs; (2) the RFP 3 scoring system already accounts for the likelihood of project success; and (3) disqualification would be contrary to the terms of RFP 3 and harm the integrity of the competitive bidding process (see Section III.G.2, above).

BECo and Altresco argue that disqualification of the DLS bid is warranted because: (1) DLS failed to provide supporting documentation for several key prices and components of its project, in violation of RFP 3 provisions; (2) DLS failed to otherwise justify several key costs and components of its project; (3) DLS cannot provide reliable power for the unrealistically low price that it bid; (4) the RFP 3 scoring system cannot adequately balance the unrealistically low price with the numerous serious viability and reliability deficiencies; (5) DLS cannot meet the terms and conditions of its proposal and the bid does not constitute a bona fide offer, contrary to the provisions of RFP 3; and (6) preservation of the integrity of the RFP 3 process requires the disqualification of any bid with an unrealistically low price (see Sections III.G.1 and III.G.3, above).

The Department found above that DLS has failed to document adequately its projected fuel costs, construction costs, financing, and overall bid price (see Sections IV.C-IV.F). BECo acknowledged that, had DLS presented adequate supporting documentation for its projected prices with its bid, the DLS proposal would have been a good project. With appropriate documentation, DLS might have been designated the winner of RFP 3.

The Department further found that, lacking adequate documentation, DLS also failed to establish that various key elements of the overall bid price were achievable or consistent

with market conditions during the RFP 3 Review Period[57] (see Sections IV.C-IV.F). Specifically, DLS failed to obtain a commitment for most of its fuel needs, underestimated its fuel commodity costs, undervalued its transportation costs, underestimated the impact of interruptibility, and used inconsistent heating values. Consequently, DLS' overall fuel supply price was inconsistent with market realities. Similarly, DLS has failed to establish that it could build its proposed plant at or below the cost contained in the pro forma in its bid, or that the project was financially sound. Because DLS failed to either document or justify these key costs, the Department finds that BECo had a reasonable basis for determining that DLS could not provide reliable power for the very low price in its bid.

Once BECo had determined that the overall price was unrealistic, it had to determine whether to score or disqualify DLS in accordance with the RFP 3 provisions. The RFP 3 scoring system was designed to balance cost, viability and reliability to maximize net benefits to ratepayers. 220 C.M.R. § 8.05(5)(c). The scoring system carefully balances price and non-price factors to compare and rank realistic proposals. BECo stated that if DLS had bid a price within the range of reasonableness, the scoring system could have accounted for the project viability risks. However, the overall bid price submitted by DLS (or any other bidder) is largely not adjustable within the RFP 3 scoring system.[58] Consequently, BECo

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[57] The Department acknowledges that it is possible for a bidder to secure a better-than-market deal in certain cost categories. Indeed, the Department encourages bidders to seek lowest cost reliable supplies. However, without adequate documentation of prices as required by RFP 3, the Department will not assume that below market prices will be obtained. Therefore, it is reasonable to assess DLS' bid against the prevailing market conditions.

[58] Within the RFP 3 scoring system, non-price factors can be verified by supporting

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determined that the DLS price factor score could not be reconciled appropriately with the low viability and reliability scores. Because BECo determined that DLS could not provide power at the price it proposed, and could not meet the terms and conditions of its proposal, BECo disqualified DLS pursuant to Section 3.8.1(n) of RFP 3.

If DLS had failed to substantiate or justify only one or two of its component costs, the credibility of the overall price might have been sufficient for BECo to score the project with deductions in appropriate scoring categories. However, the failure to substantiate or justify virtually every major cost in the proposal is not minor or technical in nature, but rather a fatal flaw. Accordingly, the Department finds that the failure of DLS to establish that its overall price and other key costs and components of its bid were realistic constituted a reasonable basis for BECo to apply Section 3.8.1(n) of RFP 3 to disqualify DLS.

Finally, the Department assesses the impact of disqualification on the integrity of the RFP process in light of the goals of the RFP process.[59] The primary goal of the RFP process is to maximize net benefits to ratepayers. Cost-effectiveness must be balanced with viability and reliability. Selection of a project with very low projected costs that is never

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[58](…continued)

documentation provided with project proposals, and scores can be adjusted if necessary to reflect verifiable facts. The price factor, however, cannot be verified in the same manner (with the exception of the emissions component). Though the overall price score could be adjusted to reflect revised emissions data from changing DLS' heating value and interruptibility assumptions, it cannot be adjusted to reflect the other problems with the fuel, construction, and financing costs discussed above. Because the price factor accounts for 44 percent of the total possible points in BECo's RFP 3, an unrealistically low price score can inappropriately skew the total results.

[59] The Department also must emphasize that the requirement that all bidders provide supporting documentation for their proposals by the bid deadline is essential to an orderly and timely review process.

financed or constructed may result in ratepayers paying higher prices for purchased power and risking capacity shortfalls. In this proceeding, the failure of DLS to substantiate or justify its unusually low prices suggests that DLS is proposing a house of cards; and a house of cards cannot generate electricity.

The Department has approved the provisions of RFP 3, including the disqualification provisions, in order to ensure that only bona fide proposals are compared and evaluated. To do otherwise would result in a process that could not maximize net benefits to ratepayers. Therefore, appropriate application of the disqualification provisions furthers the goals and preserves the integrity of the RFP process.

H. Conclusion

Accordingly, the Department finds that DLS has failed to establish that, in light of what BECo knew or should have known during the RFP 3 Review Period, BECo's decision to disqualify the DLS proposal pursuant to Section 3.8.1(n) of RFP 3 was unreasonable, and hereby concurs with BECo's disqualification of DLS.

V. ORDER

Accordingly, after due notice and consideration, it is

ORDERED: That the petition of DLS Energy, Inc. filed with the Department on June 24, 1992 be and hereby is DENIED.

By Order of the Department,

VI. CONCURRING OPINION OF COMMISSIONER BARBARA KATES-GARNICK

I am writing a concurring opinion on the denial of the DLS petition requesting the Department to reinstate its proposal to provide power pursuant to BECo's RFP 3. While I agree with the majority's conclusion that BECo had a reasonable basis for disqualifying the DLS bid, I believe that the Department should announce that it will shift either the burden of proof or the burden of production of evidence to the utility in future disqualification cases where a utility is bidding against non-utility proposals.

The discretion afforded a utility in its disqualification decisions should be differentiated from that which is allowable in scoring decisions, because there are no commensurate safeguards to ensure fair and equitable treatment of all proposals. The first problem with a disqualification decision is the lack of an evidentiary record. For example, DLS received a letter stating that it was disqualified because BECo did not think it could meet the terms and conditions of the RFP. There was no score to justify or critique and very little documentation to review.

The Department has stated that it is appropriate to allow a measure of utility discretion in administering and managing the RFP process because regulations govern most stages of the RFP process. Destec at 13. In rescoring disputes, the Department's comprehensive regulations governing the review and scoring of bids do provide adequate safeguards. 220 C.M.R. §§ 8.00 et seq. Therefore, we established a very easy standard for the utility to meet, i.e., the bidder must prove that there is no reasonable basis for the utility action. Riverside I at 19-20. I agreed with the majority that it was appropriate to apply this current standard of review for RFP disputes in the four rescoring Orders issued

earlier this year. See footnote 14 supra.

Our regulations, however, do not address disqualification nor do they provide any oversight or safeguards for disqualification decisions. Where a bidder is disqualified pursuant to a highly subjective determination that a bid is not "bona fide," or the bidder will be "unable to meet the terms and conditions of the proposal," the detailed scoring criteria that address viability and reliability and were approved by the Department are not utilized. The rules of the game cannot protect those who are not allowed to play. Even though the majority in this opinion follows the holding in MASSPOWER that otherwise cost-effective projects should not be disqualified on technicalities, there is no requirement that projects even be scored before disqualification to determine whether they might be cost-effective.[60] The Department simply has no yardstick by which to measure any disqualification decision.

One of the major purposes of the Department's regulations governing the competitive bidding process is to guard against self-dealing by the companies. See D.P.U. 86-36-G at 33-35 (1989). Because the companies will be required to bid on their own solicitations in future IRM proceedings, the possibility for self-dealing, and the need to dissuade such behavior, greatly increases. The millions of dollars that will be at stake for shareholders in an increasingly competitive power generation market will provide an inappropriate but understandable temptation to disqualify a bidder with a lower price and some viability questions but higher overall score than the utility's own bid. Again, while I agree with the

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[60] As a practical matter, we might wish to require companies to score all bidders that are disqualified to determine if such bids are "otherwise cost-effective" and to reduce the necessity for remand in case a disqualification is overturned by the Department or the courts.

majority in this case that DLS failed to substantiate virtually every major cost in its bid and that the scoring system could not account fully for the serious viability deficiencies, the current generation market is forcing bidders to cut profit margins and prices to win competitive solicitations, and inevitably this will result in more bids with viability questions. I would strongly prefer that such bids be scored rather than disqualified unless the Company can convince us, as in this case, that the scoring system cannot account for serious deficiencies and thus disqualification is warranted.

Consequently, I think it is important that disqualification decisions that may involve self-dealing be subjected to closer scrutiny than other RFP disputes. This could be accomplished without changing the reasonableness standard of review by either (1) shifting the burden of proof to the company, or (2) shifting the burden of production of evidence while leaving the burden of proof on the petitioner. I support shifting the entire burden of proof to the company in disqualification cases, while preserving the broad reasonableness standard of review. Alternatively, and at a minimum, I believe that shifting the burden of production is necessary and appropriate.

The device of shifting the burden of production is used in other legal contexts under similar circumstances, notably employment discrimination cases,[61] and unfair labor practice cases.[62] Discrimination cases provide an apt analogy to bidder disqualification disputes, because: (1) the party making the disqualifying decision, whether to refrain from hiring or

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[61] See McDonnell Douglas Corp. v. Green, 411 U.S. 792 (1973).

[62] See Trustees of Forbes Library v. Labor Relations Commission, 384 Mass. 559 (1981).

promoting, or to disqualify a bidder, traditionally has been afforded a great amount of discretion in that decisionmaking; (2) courts have been reluctant to substitute judicial judgment for the judgment of a decisionmaker with expertise in the field; and (3) the decisionmaker is in possession of or has superior access to the information needed by the party challenging the decision.

In a case involving the shifting of the burden of production, an aggrieved bidder first would be required to show that the bidder was arguably qualified, did in fact enter a complete bid, and was subsequently disqualified by the utility. At this stage in the proceeding, the aggrieved bidder is presenting evidence within its control.

Once the aggrieved bidder established this prima facie case of improper disqualification, the burden of production of evidence would shift to the company.[63] The company then would be required to articulate a legitimate basis for its decision.

Finally, the aggrieved bidder would have the opportunity to prove that the reasons proffered by the company for its disqualification decision were not the real reasons for the company's decision, but were merely pretextual. The aggrieved bidder would carry the full burden of proof to establish that there was no legitimate reason for the company's decision.

I strongly recommend that the Department shift the burden of proof or burden of production for disqualification disputes in future IRM solicitations where utility proposals will be competing directly against other bidders. I think this is necessary to protect against self-dealing and the disqualification of otherwise valid and cost-effective supply options.

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[63] The burden of proof would remain with the petitioner at all times under this proposed standard.

Only by protecting the integrity of the competitive solicitation process can the Department ensure that companies seek and secure the most reliable least-cost power available.

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Barbara Kates-Garnick
Commissioner

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