ANNEXE 2

RAPPORT DU CONSULTANT MERRIMACK ENERGY GROUP INC.

Assessment of Hydro-Quebec Distribution's Call for Tenders Process for Energy Produced by Biomass Cogeneration for a Total of 125 MW of Firm Capacity and Associated Energy

A/O 2009-01

Final Report

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Prepared by
Merrimack Energy Group, Inc.

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I. Introduction

Merrimack Energy Group, Inc. (Merrimack Energy) has served as Independent Consultant to Hydro-Quebec Distribution (Hydro-Quebec or "Company") to assist Hydro-Quebec Distribution with the bid evaluation and selection process associated with the 125 MW Biomass Cogeneration Call for Tenders (A/O 2009-01). As Independent Consultant, the role of Merrimack Energy in the process has included the following: [1]

- Provide independent input and advice on issues requested by Hydro-Quebec Distribution based on Merrimack Energy's experience in other competitive solicitation processes throughout North America for renewable and conventional resources. [2]

- Review the detailed evaluation criteria, evaluation results, and documentation developed and utilized by Hydro-Quebec Distribution's evaluation team to complete the assessment of each bid to ensure that there is consistency in how the scoring of bids was undertaken.

- Conduct an independent assessment of the price and non-price evaluations of all the bids received to ensure that Hydro-Quebec Distribution's bid evaluation process is fair, equitable, consistent and unbiased.

- Serve as a member of the Call for Tenders Committee.

- Conduct research, as required, on key issues based on industry practices from other jurisdictions.

This report addresses the activities associated primarily with the bid evaluation and selection stages of Hydro-Quebec Distribution's Call for Tenders (A/O 2009-01) for the purchase of 125 MW of capacity and associated energy produced by biomass cogeneration in Quebec. The objective of this assessment is to comment on the fairness and consistency of the bid evaluation and selection process. The assessment will focus on the Call for Tenders procedures and evaluation processes and their consistency with the requirements of Hydro-Quebec Distribution's Biomass Cogeneration Call for Tenders and with general industry standards for similar competitive solicitation processes. The report primarily addresses the three steps of the evaluation and selection process,

[1] The scope of the mandate for services for Merrimack Energy ends at the conclusion of the Step 3 evaluation and does not include contract award.

[2] The Principal of Merrimack Energy and Project Manager for this assignment has served as Independent Evaluator or Monitor on over thirty competitive procurement assignments and has assisted utilities and other power buyers in nearly fifty major procurement processes, conducting independent evaluation and review of hundreds of power supply proposals for renewable and conventional resources.

including (1) minimum requirements, (2) ranking of bids based on the cost of electricity and non-price criteria, and (3) simulation of bid combinations to determine the lowest overall cost.

This report also focuses largely on the role and activities performed by Hydro-Quebec Distribution's Evaluation Team during the bid evaluation and selection process, leading to the selection of the preferred projects.

For purposes of undertaking this assessment of the Biomass Cogeneration Call for Tenders process and procedures associated with the evaluation and selection of bids, the following issues will be addressed in this report:

1. A summary and overview of the major aspects of the Call for Tenders;

2. A discussion of the various steps or activities in the bid evaluation process as defined in the Call for Tenders documents and related documents, including a discussion of the requirements of the Biomass Cogeneration Call for Tenders;

3. A general description of how the bid evaluation process and procedures were carried out by Hydro-Quebec Distribution. Included in this assessment will be (1) a description of the key tasks; (2) the roles of Hydro-Quebec Distribution's Evaluation Team and the role of Merrimack Energy in the process; (3) procedures undertaken to complete the evaluation; (4) documentation prepared by Hydro-Quebec Distribution to support the bid evaluation process; and (5) issues raised during the evaluation process.

4. An overall evaluation of the performance of Hydro-Quebec Distribution in completing these stages of the process.

The overall bid evaluation process and procedures required are identified in the "Call for Tenders and Contract Award Procedure". The Call for Tenders document and associated addendum further explains the process and procedures as implemented, as well as the evaluation criteria. This document effectively establishes the "rules of the game" and the requirements of bidders for competing in this process. In general, the process and procedures followed by Hydro-Quebec Distribution are generally similar to the process followed in other Calls for Tenders. The adjustments made to this Biomass Cogeneration Call for Tenders (A/O 2009-01) will also be highlighted in this report.

II. Summary and Overview of the Call for Tenders

Through this Call for Tenders (A/O 2009-01), Hydro-Quebec Distribution seeks to award contracts for the supply of electricity generated in Quebec from new cogeneration plants using biomass for a total of 125 MW of installed capacity. The term of the contract may not be less than fifteen (15) years or more than twenty-five (25) years starting from the commencement of deliveries. The commencement date of deliveries shall be no later than December 1, 2012.

The process was initiated with issuance of the Call for Tenders Document (A/O 2009-01) on April 14, 2009. A pre-bid conference was held on July 8, 2009. The Call for Tenders Registration Form (Notice of Intent to Bid) was due on October 1, 2009 and proposals were due on October 20, 2009.

A bid may be for all or a portion of the target requirements of 125 MW, and there is no minimum quantity. The electricity must originate from new generating facilities located in Quebec and may be installed in new or existing buildings. The process steam must be used by a company located in Quebec. In addition, the biomass used in the new cogeneration plant must account for at least 75% of the fuel used to generate the power plant's electricity.

Hydro-Quebec Distribution's objective is to evaluate the bids received and choose, among the best bids, the projects that offer electricity at competitive prices by selecting a combination of bids that will result in the lowest cost in $/MWh.

The eligibility requirements of this Call for Tenders are unique in a number of ways, due primarily to the requirements for cogeneration and eligible fuel requirements. Some of the primary eligibility requirements include:

- The electricity must originate from new generating facilities located in Quebec;
- The process steam must be used by a company located in Quebec;
- The energy content of the process steam cannot be less than 10% of the energy content of the total annual generation of electricity and process steam of the cogeneration plant;
- The electricity generation process proposed by the bidder must have attained proven technological maturity and the strategic generating equipment (e.g. turbines, generators, boilers) must be commercially available;
- The biomass used in the new cogeneration plant must account for at least 75% of the fuel used (on a calorific base) to generate the plant's electricity. Electricity and process steam share the same energy content of biomass in proportion of cumulative energetic content of all fuels used in the power plant;
- Eligible biomass as a fuel includes:
    - Residual forest biomass;
    - Biodegradable residual materials rejected or not accepted following reclamation activities and intended for disposal in landfill sites or incinerators;

- Recovered biodegradable residual materials for which other reclamation methods are not subject to economically viable technology.

Bidders are required to submit their pricing for energy only. There is no payment for capacity. Pricing formulae involving a fixed-cost component (e.g. $/month) are not admissible. The Call for Tenders allows bidders to split their pricing formulas into multiple components and to index each component by a specific allowable index to match the costs and revenues associated with the project.

It is important to note that this Call for Tenders process is effectively a targeted solicitation process, open only to a specific type of resource (i.e. biomass cogeneration). Thus, issues associated with fairness and equity in the process will be limited to treatment of individual bidders, not to different types of resources, technologies, project sizes, etc. As a result, these issues will be addressed in this report from the perspective of the unique nature of this solicitation.

However, many of the other requirements of the Call for Tenders are consistent with industry practices, including the overall evaluation process, threshold criteria, a number of the evaluation criteria, requirements of bidders, and contract provisions. These issues will be discussed in the next section of this report.

III. Description and Implementation of the Biomass-Generated Electricity Call for Tenders Bid Evaluation Process

A. Description of the Bid Evaluation and Selection Process

The bid evaluation and selection process followed in this Call for Tenders was clearly identified in the Call for Tenders document and is similar to the process followed in other Calls for Tenders issued by Hydro-Quebec Distribution, including the three major steps of (1) minimum requirements; (2) ranking of bids based on the cost of electricity and non-price criteria; and (3) simulation of bid combinations to determine the lowest overall cost. As will be discussed, the first two steps were very similar to other Hydro-Quebec Distribution Calls for Tenders, although the criteria developed for this process were specific for this Call for Tenders.

This Chapter of the Report will also provide an overview of the response to the Call for Tenders and identify decisions made at each stage of the process to arrive at a final selection of bids or bid combinations.

As a brief background, the Call for Tenders process for a total of 125 MW of installed biomass cogeneration capacity was a reasonably competitive process, although the amount of capacity received was less than the amount requested. There were 10 submissions provided by seven bidders.

Step 1 of Evaluation Process: Minimum Requirements

As noted, ten submissions were received prior to or at the deadline of October 20, 2009 established in the Call for Tenders. Bid opening took place on October 21, 2009 as scheduled.

Consistent with other Calls for Tenders, upon receipt of the bids, all proposals would be subject to a completeness check. The evaluation team would review the bids to determine if there were any breaches which would automatically result in disqualification.[3]

In the Step 1 process subsequent to the initial completeness check, the evaluators shall conduct a more detailed review of the bids to determine if there was missing information or if any information presented by the bidders needed further clarification or raised additional questions for follow-up. Any bid deemed frivolous or non-conforming would be disqualified.

Also included during Step 1 in the evaluation process was the evaluation of bids to ensure they conformed to the minimum requirements listed in the Call for Tenders. At this stage, bidders received clarification and follow-up questions from Hydro-Quebec Distribution on a range of issues, if necessary.

[3] Some of the breaches which automatically disqualify a bid include late submission, the bidder is not registered, and the bid was not signed by an authorized person.

The minimum requirements were expanded in this Call for Tenders to account for the unique requirements of this Call for Tenders. The identified minimum standards included:

1. Identification of the site for the proposed project and demonstration of control over the site. The site shall be located in Quebec and must be capable of being connected to Hydro-Quebec's integrated system. The bidder must provide a copy of the title or documents confirming that the bidder owns the land or has acquired the right to use it. If the bidder does not own or control the site, the bidder must have at least a letter of intent from the landowners dealing with the acquisition of such rights;

2. The bidder must have identified at least one buyer for the process steam and provide, at the least, a letter from the future steam host confirming the agreement;

3. The bidder or its affiliates must demonstrate experience in the development or operation of at least one similar commercial electricity generation project;

4. Demonstration of technological maturity of the generation technology proposed consistent with the requirements of the Call for Tenders;

5. It must be possible to complete all the work necessary to interconnect and to integrate the generation equipment proposed by the bidder to Hydro-Quebec's integrated network in time to meet the date requested by the bidder for the initial energizing of the switchyard. Hydro-Quebec Distribution shall rely on Hydro-Quebec TransEnergie's evaluation of the initial energizing date for each bid;

All the information necessary to evaluate the bids from the perspective of meeting minimum requirements was requested in the Bid Form included as Appendix 10 (Bid Form) in the Call for Tenders document. Hydro-Quebec TransEnergie was responsible for making the determination whether the proposal could meet the required energizing date requested by the bidder. Hydro-Quebec TransEnergie, therefore, reviewed and evaluated sections of the bids pertaining to this information.

One bid was eliminated at this stage in the process for failure to demonstrate site control consistent with the requirements of the Call for Tenders. Merrimack Energy agreed with the decision of Hydro-Quebec Distribution to eliminate the bid after providing the opportunity to the bidder to demonstrate its control of the project's site.

Step 2: Ranking of Bids

In Step 2 of the bid evaluation process, all bids that met the minimum requirements criteria were subject to evaluation based on the criteria listed in Exhibit 1 below, which are included in the Call for Tenders document.

Exhibit 1
Evaluation Criteria

Criteria	Weighting
i. Cost of electricity	40
ii.Sustainable development, which included: (a) Minimizing greenhouse gas emissions (b) Maximizing the generation of process steam (c) Support of local elected representatives (d) Accredited environmental management system	32
iii. Financial Capability	10
iv. Project Feasibility	11
v. Relevant Experience	7
Total	100

In addition, there were several sub-categories within each of the major categories listed in Exhibit 2. For example, the sub-categories included in project feasibility include: (1) timing of interconnection to the grid; (2) master plan for realization of the project; (3) supply plan for biomass and secondary fuels; and (4) environmental permitting. Furthermore, Appendix 10 (Bid Form) in the A/O 2009-01 Call for Tenders provided a list of questions, information required to be submitted by the bidder in their proposal, and in some cases forms for completing and incorporating such information in the proposal.

The Call for Tenders also described each criterion and the important characteristics of each criterion for consideration by the bidder. The evaluation criteria were therefore transparent in the process and all bidders knew the criteria on which they would be evaluated and the weights afforded to each of the major criteria.

The evaluation criteria can be classified as price and non-price related criteria. For example, the Cost of Electricity can be classified as a price-related criterion, while the other criteria are all non-price related.

Within the non-price evaluation categories, individual team members were responsible for conducting the evaluation of all bids within their specific area of expertise. A second

evaluator was assigned to each of the criteria to provide support and verify the results, if needed. The objective of this process was to ensure that all proposals were evaluated consistently. Each bid would be evaluated based on each of the criteria using the evaluation sheets developed by the Evaluation Team.

The price evaluation (i.e. Cost of Electricity) in this stage of the process was designed to compare each bid based on the proposed pricing formulas offered by the bidder and the quantity of contract energy offered. Hydro-Quebec Distribution used a real levelized cost methodology approach for evaluating each bid. Under this methodology each component in the bidders' price formula was projected based on the pricing formula and the forecast of the specific index proposed by the bidder for each pricing component. The annual cash flow of the costs over the entire term of the contract were calculated and discounted in 2009 dollars, and are then expressed as a unit cost of electricity ($/MWh) using the contract energy (guaranteed energy on an annual basis) provided in Section 2.1.2 of the Bid Form. This approach therefore took into account the pricing formulas and components submitted by the bidders as well as the quantity of contract energy offered by the bidder in estimating the total annual unit cost of electricity and yearly discounted cash flows. This results in a real levelized cost in 2009 dollars per MWh for all bids which allows for a consistent evaluation. Hydro-Quebec Distribution used its forecasts of inflation and other indices, and its discount rate to estimate the long-term cost of power for each proposal. Forecasts of the index values were developed by an independent firm before bids were submitted.

In addition, applicable transmission costs were included in arriving at the price of energy for each proposal. At this stage in the process, the applicable transmission costs include:

- The cost of connecting the power plant to the regional transmission system or distribution system, including the cost of modifying the regional system lines and substations and, if applicable, the curtailment cost;
- The cost of the power plant's switchyard;
- Electrical loss rate associated with the power plant's generation;
- Cost of reinforcing the bulk transmission system investments as a result of adding new power plants (step 3 only);
- Avoided costs associated with any future transmission system investments.

The applicable transmission cost is estimated on the basis of a summary study conducted by Hydro-Quebec TransEnergie.

Thus, each proposal would be evaluated using the same set of assumptions for each of the indices included in the proposal's pricing formula. Furthermore, since bidders did not have access to the forecast of input assumptions, bidders had to present their preferred pricing proposals rather than attempt to "game" their bids relative to the inputs.

The result of this analysis would therefore be a single unit price of power (i.e. the real levelized cost, which is the price in the base year, which, if escalated by inflation, provides the same net present value price stream as the pricing formula proposed by the

bidder). The 40 monetary points were awarded based on the relative cost of each bid to the lowest cost bid, with the lowest cost bid receiving the maximum 40 points. The bid that comprises the highest cost receives 8 points. All other bids are attributed points based on the linear function between the two extremes.

The bids would therefore be evaluated and scored relative to the evaluation criteria and associated weights given in the Call for Tenders. The rankings of each bid at this stage of the evaluation would be determined based on the total points obtained for all the criteria.

At this stage in the process, one bid was not compliant with a zoning by-law but the bidder demonstrated that the municipality was supportive of the project and started the needed modification of the zoning by-law. This demonstration allowed the bidder to remain in conformance with the requirements of the Call for Tenders. In anticipation that the municipality was acting diligently to solve the issue, the remaining nine bids were subject to the price and non-price evaluation during Step 2 in the process. All remaining bids were deemed eligible at this stage with no need to eliminate any bids.

Step 3: Simulation of Bid Combinations

The next step in the evaluation process is the simulation of bid combinations. In this stage of the evaluation, it is the intent of Hydro-Quebec Distribution that various combinations of bids are formed using the best bids identified and ranked in Step 2 to form the targeted block of 125 MW.

The combination of bids would be assessed in detail in order to identify the combination with the lowest total cost in $/MWh, including the impact on applicable transmission costs.

In this stage of the evaluation, all applicable transmission costs would be included in the analysis for each portfolio. The analysis regarding transmission costs was to be completed by Hydro-Quebec TransEnergie based on the bid combinations/portfolios provided by Hydro-Quebec Distribution.

Since the amount of capacity offered was less than the amount requested there was not need to undertake a bid combinations assessment. Instead, Hydro-Quebec Distribution ranked and selected resources based on a comparison of the real levelized cost of the bids offered (without transmission) to a benchmark of biomass options. The primary benchmark used for comparison was the long-term cost of biomass determined by the Ontario Power Authority (“OPA”) for purposes of implementing its Feed-in Tariff program. Since it is difficult to develop a standardized benchmark for biomass generation options, Merrimack Energy felt that the use of the biomass benchmark from the OPA Feed-in tariff program was a reasonable benchmark given the level of experience of OPA with generation costs for a variety of technologies and the level of effort required to develop and implement OPA’s Feed-in tariff program.

As described in Hydro-Quebec's press release of December 18, 2009 eight bids were accepted for a total of 60.7 MW, with an average price of $108/MWh (not including transmission).

B. Implementation of the Bid Evaluation Process

This section of the report describes the actual implementation of the bid evaluation and selection process. This includes identifying and describing the organization of the Evaluation Teams and procedures established by Hydro-Quebec Distribution, the roles and activities of the Hydro-Quebec Distribution's Evaluation Team, the role and activities of Merrimack Energy, and an evaluation of the three steps of the evaluation and selection process.

Management Structure and Organization

The team responsible for evaluating the bids was managed by the Director, Electricity Supply (Director), who was in charge of implementing the bid evaluation process and of assigning personnel for this purpose. He was responsible for ensuring compliance with the process and of supervising communications with consultants, bidders, and other divisions of Hydro-Quebec involved in the process.

The Energy Supply Manager (Manager) assisted the Director of Electricity Supply. He was responsible for maintaining the bid evaluation documentation and was the coordinator for the bid evaluation Project Team. The team is comprised of Hydro-Quebec Distribution personnel and consultants. The consultants, Deloitte Inc. and Merrimack Energy shall also take part in the bid evaluation process. For example, requests for information from bidders had to be approved by the Manager before being sent to Deloitte Inc. The Manager was responsible for coordinating with Deloitte Inc. who transmitted such requests to the bidders.

As was the case with other Call for Tenders, one of the most important aspects of the solicitation process was that the methodologies and criteria underlying the bid evaluation process (Steps 1 and 2) were developed by Hydro-Quebec Distribution prior to receipt of bids and identified to bidders either in the Call for Tenders documents or Addendum to the Call for Tenders. The solicitation process conducted by Hydro-Quebec Distribution is a very transparent process, with a level of transparency that exceeds the levels in most other competitive procurement processes.

Project Team members responsible for bid evaluation were also involved in designing the criteria and detailed evaluation methodologies for their specific categories. The criteria underlying the evaluation process were developed to be consistent with the type of resource requested and the unique considerations underlying the biomass cogeneration Call for Tenders.

A representative of Hydro-Quebec Distribution's Project Team was assigned to each specific criterion. The representative was required to evaluate each bid relative to the

same criteria to ensure consistency of the evaluation. A Bid Evaluation Guide was developed prior to receipt of bids and served as an important reference and documentation during the evaluation process. [4]

The role of Merrimack Energy in the process was defined as reviewing and evaluating the documentation prepared and used by members of the Evaluation Team to complete all steps of the evaluation process to ensure consistency in the results. Merrimack Energy was primarily responsible for the technical issues associated with the evaluation process, including review and assessment of the minimum requirements evaluation, the price evaluation, and the non-price evaluation. Merrimack Energy staff therefore participated in the review and evaluation of the bids from the perspective of both the price and non-price categories.

Consistent with the procedures followed in other Calls for Tenders, Hydro-Quebec Distribution organized a Call for Tenders Committee comprised of the President of Hydro-Quebec Distribution, the Director of Electricity Supply, the Manager for Energy Supply, legal staff and other members of the project team, and representatives from Deloitte Inc. and Merrimack Energy. The Committee met three times during the bid evaluation and selection process to discuss the status of the process and address any issues that arose with regard to the bid evaluation and selection process. The meetings of the Committee were generally held at or around the completion of a specific Step in the process to review and discuss the status and completion of that Step.

Bid Evaluation Process

As noted, bids were received on October 20, 2009 and were publicly opened on October 21, 2009. No bids were initially rejected at bid opening. As previously noted, one bid was rejected at the threshold stage due to failure to demonstrate site control. Another bid which had a zoning issue was able to resolve the issue and remained in the process.

Merrimack Energy met with the Energy Supply Manager to discuss the Company's decisions regarding bid eligibility in the compliance stage of the evaluation as well as the Minimum Requirements assessment and agreed with Hydro-Quebec's decision regarding bid eligibility.

In the second step of the process, Hydro-Quebec Distribution undertook a detailed price and non-price evaluation of the remaining bids and variants, consistent with the evaluation criteria identified in Exhibit 1 of this report. The price aspects (i.e. cost of electricity) and non-price aspects of the evaluation proceeded on parallel paths as well, with separate team members responsible for the price and non-price evaluation.

Cost of Electricity (Price Evaluation)

[4] A draft of the Bid Evaluation Guide was provided to Merrimack Energy by the Energy Supply Manager for comment and a final copy was provided prior to receipt of bids.

From the price evaluation perspective, a "check and balance" process was built in to ensure the bids were fairly and consistently evaluated. Hydro-Quebec's price evaluation team conducted its assessment based on the bidders pricing formula, utilizing its own model and standard assumptions to estimate the real levelized cost of energy for each proposal. Merrimack Energy also conducted its own assessment of the bids based on its interpretation of the pricing formula and using its own model. The internal Hydro-Quebec analysts and Merrimack Energy used the same assumptions and indices as allowed by Hydro-Quebec Distribution in Appendix 5 of the Call for Tenders document.

As noted, Merrimack Energy evaluated all the bids using the same set of input forecasts but a different model developed by Merrimack Energy. The initial evaluation revealed that Merrimack Energy's results were generally slightly higher than Hydro-Quebec's analysis. After review, it was determined that the reason for the difference was attributed to the cash flow discounting methodologies used. However, the differences were consistent and the ranking of the bids was the same.

It is also noteworthy that the Pricing Form contained in Section 2 of the Bid Form was very effective in generating consistent information from the bidders with little need for interpretation of the pricing formulas. The pricing proposals submitted by the bidders could easily be interpreted and evaluated by the analysts at Hydro-Quebec and Merrimack Energy. Also, it was clear that bidders were able to effectively complete the pricing forms, with minimum follow-up requests for information necessary.

Non-Price Evaluation

All eligible bids were also evaluated by Hydro-Quebec Distribution's non-price evaluation team using the established evaluation criteria and weights as the basis for the evaluation, as well as the methodology described in the Bid Evaluation Guide.

For the non-price evaluation, project team members were assigned to specific criteria and were required to evaluate all bids relative to the specified criteria. Several members of the team also developed more detailed and comprehensive criteria to ensure the projects could be effectively distinguished within their specific criteria. Project team members completed an initial evaluation of the bids based on the established criteria. The Project Manager from Merrimack Energy also read the bids and focused on the information required to evaluate the bids relative to each criteria.

Subsequent to Merrimack Energy's review, a Merrimack Energy representative and Hydro-Quebec Distribution's project team members met to review and discuss the detailed criteria applied by Hydro-Quebec Distribution, the results of the evaluation within each category and justification for the evaluation. The detailed evaluation sheets were provided to Merrimack Energy during the initial bid review and evaluation discussions. Merrimack Energy generally considers its role in assessing the non-price evaluation in this and other similar processes as "challenging" the utility's evaluation to ensure the results are thorough and consistent. As a result of these meetings and discussions, in some cases certain aspects of the evaluation went through a reassessment

of the evaluation results before final assessments were complete. This served to ensure that the evaluation process was fair and consistent, and all reasonable information was accounted for in conducting the evaluation.

The objective of this process was to ensure that a consistent evaluation of each bid was achieved. While Merrimack Energy raised some questions to test the evaluation process and methodology, we recognized the comprehensiveness of the evaluation undertaken by Hydro-Quebec's evaluation team and were in agreement with the final non-price evaluation and with the final scores developed by Hydro-Quebec Distribution. In addition, Merrimack Energy's view was that the level of effort, level of detail and thoroughness of the evaluation completed by all non-price team members was very comprehensive. In addition, we found the documentation to support the evaluation to be detailed.

After the price and non-price scores were compiled, the bids were ranked on the basis of total score. Transmission cost impacts were included in the ranking.

As a result of the analysis of bids along with comparison of the bid prices to a biomass benchmark price based on the Ontario Power Authority's Feed-in tariff program Hydro-Quebec Distribution selected eight projects with which to execute a contract. The average price of the contracts as well as the price range, in our view is competitive with the current price of biomass generated electricity in other regions of the United States and Canada based on our review of the Feed-in tariff rates in Ontario and Vermont as well as the cost of biomass reported in studies in California (which has a significant biomass requirement and interest) and other areas.

IV. Framework and Principles for Evaluating Hydro-Quebec Distribution's Performance in the Bid Evaluation and Selection Process

This Biomass Cogeneration Call for Tenders (A/O 2009-01) is classified as a targeted solicitation process limited to a specific resource. Based on Merrimack Energy's experience with competitive bidding processes and observations regarding such processes, the key areas of inquiry and the underlying principles used by Merrimack Energy to evaluate the bid evaluation and selection process include the following:

1. Were the solicitation targets, principles and objectives clearly defined?

2. Did the solicitation process result in competitive benefits from the process?

3. Was the solicitation process designed to encourage broad participation from potential bidders?

4. Did Hydro-Quebec Distribution implement adequate outreach initiatives to encourage a significant response from bidders?

5. Was the solicitation process consistent, fair and equitable, comprehensive and unbiased to all bidders?

6. Were the bid evaluation and selection process and criteria reasonably transparent such that bidders would have a reasonable indication as to how they would be evaluated and selected?

7. Did the evaluation methodology reasonably identify how quantitative and qualitative measures would be considered and applied?

8. Did the Call for Tenders (i.e. Call for Tenders document, the Bid Form, and Standard Contract) describe the bidding guidelines, the bidding requirements to guide bidders in preparing and submitting their proposals, and the bid evaluation and selection criteria.

9. Did the utility adequately document the results of the evaluation and selection process?

10. Did the solicitation process include thorough, consistent and accurate information on which to evaluate bids, a consistent and equitable evaluation process, documentation of decisions, and guidelines for undertaking the solicitation process.

11. Did the solicitation process ensure that the Power Purchase Agreement was designed to minimize risk to the utility customers while ensuring that projects selected can be reasonably financed.

12. Did the solicitation process incorporate the unique aspects of the utility system and the preferences and requirements of the utility and its customers.

The implementation of the 125 MW Biomass Cogeneration Call for Tenders process relative to the characteristics identified previously is described below. Merrimack Energy has not been involved in the contract preparation process and is thus not in a position to discuss this objective.

1. Solicitation Targets

The Call for Tenders document clearly defined the amount of capacity requested, the timing for providing the capacity, the type of products and product characteristics required, the duration of the contract, bidder eligibility, and the context of the Call for Tenders with regard to the Quebec Government mandate.

2. Competitive Benefits

The solicitation process encouraged a modest response from the market, with 10 different proposals offering less capacity than the amount solicited. In addition, with one exception, the bidders were not well financed or experienced. The majority of the proposals were not very mature. However, the prices of the bids selected were generally competitive with market benchmarks for similarly sized projects.

3. Broad Participation from Potential Bidders

As noted above, the process encouraged a modest response from smaller, less experienced developers. The level of interest from the market was disappointing but overall was consistent with the response from the first Biomass Call for Tenders where the level of response was also lower than the amount of capacity requested.

4. Outreach Initiatives

Hydro-Quebec has done a very effective job of maintaining communications with bidders through their website which is bidder friendly and accessible. The availability of documents, questions and answers, and notifications about the process allow bidders to maintain accessible contact. The integration between the Quebec Government, the Company and the Regie has served to effectively “advertise” the process.

5. The solicitation process should be consistent, fair and equitable, unbiased, and comprehensive

This principal focus of our assessment of Hydro-Quebec Distribution’s Call for Tenders process and the Company’s performance in carrying out the process was on the bid evaluation and selection process. The key criteria (fair, equitable, consistent and unbiased) are applied to Hydro-Quebec Distribution’s implementation of the evaluation

and selection process as well as Hydro-Quebec Distribution's ability to adhere to the requirements outlined in the Call for Tenders document and associated Addendum. Therefore, the critique will focus on the implementation of the process rather than specific issues regarding the process.

In our view, Hydro-Quebec Distribution's evaluation and selection process was consistent throughout. From a non-price perspective, the approach of requiring individual team members to evaluate specific criterion for all bids ensures that bids should be consistently evaluated since the evaluator has the opportunity to not only evaluate one specific criterion in conjunction with their expertise but to review the relative scoring of each bid within the established criterion. Merrimack Energy's independent review of the evaluation confirms that the bids were consistently evaluated from a non-price perspective.

In additional, the level of detail and comprehensiveness of the non-price evaluation continues to be exemplary.

The price evaluation methodologies were designed to evaluate bids using the same or consistent set of input parameters and assumptions. In addition, the real levelized cost analysis applied in Step 2 is an excellent methodology for comparing bids of this nature (i.e. similar resources) on a consistent basis. To ensure consistency in the evaluation, two separate analyses were conducted, one by Hydro-Quebec Distribution and one by Merrimack Energy. The results of the evaluation indicated a consistent evaluation of the bids since the results were very close and differences could be explained. While the analysis results were not an exact match, the ranking of bids was the same since differences in the analysis were consistent for all bids..

With regard to bias, the most obvious consideration is whether the process favors one type of bidder over another. Since all bids were for a similar type resource (and technology) any presence of bias would likely be in the implementation of the process itself, rather than the criteria or other information that could affect different bidders. Based on our direct involvement in the process, we could find no examples where one bid was more favorably treated than another. First, the presence of Deloitte Inc. as Official Representative and its role as link between Hydro-Quebec Distribution and the bidder ensures that all bidders have access to the same information at the same time. In addition, the process was a fairly open process with information pertinent to all bids provided on the Website for review. Hydro-Quebec Distribution responded to large number of questions from bidders and posted all responses on the Website in a timely manner. The Call for Tenders was also designed to explain in detail the evaluation process, the requirements of Hydro-Quebec Distribution, and the information that all bidders were required to submit.

We do not believe any bid had an inherent competitive advantage within the parameters of the Call for Tenders. The non-compliance assessment and follow-up information requirements ensured all bidders provided the same information for evaluation purposes.

Also, Hydro-Quebec Distribution was focused on ensuring that all bidders competed on an equal footing and had access to the same information.

The Call for Tenders process was well structured to ensure that the information required in the Call for Tenders document was linked to the evaluation criteria. Hydro-Quebec Distribution requested a considerable amount of information from the bidder to gain an in-depth assessment of the proposed project and utilized all the relevant information to evaluate and score the bid.

The thoroughness of the evaluation criteria also enhanced the ability of Hydro-Quebec Distribution to develop a comprehensive database and information support to back-up the non-price and price related evaluation. Merrimack Energy reviewed the non-price and price evaluation documentation and recognizes the thoroughness of the documentation process.

6. Transparency of the Process

The Call for Tenders documents and responses to questions led to a process where bidders would be aware how to effectively compete. The overall weights of each criterion were provided as well as a description of the requirements within each criterion. The information required of bidders was clear and concise as witnessed by the very complete and consistent proposals submitted by bidders.

7. Application of Quantitative and Qualitative Measures

The Call for Tenders document clearly articulated the quantitative and qualitative techniques and requirements associated with the evaluation process. The methodologies were described in the Call for Tenders. Also, the pricing evaluation sheets were clear and easy to use as illustrated by the limited errors associated with completing these forms. Hydro-Quebec also provided bidders the opportunity to suggest various indices that could allow bidders the opportunity to match their costs with the indexed pricing in their bids. Such indexing opportunities provided bidders with the ability to minimize market risk in their pricing proposals by matching their costs to the revenues received from the output of their project.

8. The Call for Tenders Documents should describe the process clearly and provide adequate information on which bidders could complete their proposals

This objective deals with the quality of the documents contained in the Call for Tenders package (i.e. Call for Tenders, Standard Contract, and Bid Form) and the integration among the documents. Hydro-Quebec Distribution's Call for Tenders provided considerable detail regarding the information required of bidders, the basis for evaluation and selection, and the criteria of importance. The Call for Tenders process clearly provides a direct link between the Call for Tenders document, bid form and standard contract.

9. Documentation of Results

Based on our review, it is obvious that all evaluators maintained very detailed information to support their evaluation of the bids. This included information contained in the bids, third-party information, and supporting information provided by other groups within the Company.

10. The solicitation process should include thorough, consistent, and accurate information on which to evaluate bids

The bid form requires a significant amount of information that bidders must include in their proposals. Under Hydro-Quebec's evaluation process, the vast majority of this information is used in the analysis and is consistent with the evaluation criteria developed. The level of information provided ensured that Hydro-Quebec Distribution could undertake a consistent and comprehensive analysis of each proposal and reflect the individual attributes of each proposal in the evaluation. Our review and evaluation found that Hydro-Quebec's evaluation and selection process was a thorough and comprehensive assessment. Every "point" was scrutinized in the evaluation and the internal evaluation criteria on which the analysis was based were carefully and expertly developed to ensure that bids characteristics could be distinguished. We found no biases in the evaluation criteria or process and the documentation to be very thorough.

V. Conclusions

The objective of this assessment is to comment on the fairness and consistency of the bid evaluation and selection process for the purchase of energy produced by cogeneration biomass in Quebec via Call for Tenders A/O 2009-01 for a total of 125 MW of firm capacity. The assessment will focus on the Call for Tenders procedures and evaluation processes and their consistency with previous Hydro-Quebec Distribution Call for Tenders and with general industry standards for similar competitive solicitation processes.

In the opinion of Merrimack Energy, the bid evaluation and selection process was undertaken by Hydro-Quebec Distribution in a fair, consistent and comprehensive manner, with all bids treated fairly and equitably. Furthermore, the bid evaluation and selection process was consistent with industry standards for similar procurement processes. A list of important aspects of the Call for Tenders bid evaluation and selection process is provided below.

1. The Call for Tenders Document (A/O 2009-01) was a detailed and transparent document that clearly identified the unique nature of the solicitation process, the products requested, the information required of the bidders, and the bid evaluation and selection process.

2. The three-stage evaluation process utilized by Hydro-Quebec Distribution (i.e. Evaluation of bids as per the minimum requirements, Ranking of Bids, and Simulation of Bid Combinations) outlined in the Call for Tenders is, in substance, consistent with the approaches followed by other utilities. In particular, the use of pricing analysis as the final criteria for selection of the preferred combination of bids is common practice in the industry.

3. The price analysis undertaken in Step 2 assessed each proposal based on the pricing formulas proposed by the bidder. The analysis used the same consistent set of economic assumptions and forecasts of indices proposed by bidders in their proposals, thus ensuring that all bids were fairly and consistently evaluated. All eligible bids were assessed in the second stage of the evaluation using a typical price evaluation methodology (i.e. real levelized cost analysis) standard in the electric utility industry.

4. All proposals that passed the Minimum Requirements stage (i.e. Step 1) were thoroughly and consistently evaluated and ranked based on a detailed price and non-price assessment. All evaluation scores were thoroughly scrutinized by Hydro-Quebec Distribution's bid evaluation team and Merrimack Energy. Merrimack Energy conducted an independent Step 2 price evaluation using its own model for all proposals. The results of Merrimack Energy's analysis for each bid were consistent with the results of Hydro-Quebec Distribution's assessment, with the difference largely explained by a slight difference in the methodology for determining contract year start dates and indexing periods.

Merrimack Energy's results illustrated there were no systematic biases in the evaluation and indicated a consistency in interpreting the bid price formulas.

5. Hydro-Quebec Distribution followed an approach to bid evaluation that included auditing of the results of several non-price criteria by members of the Company's Evaluation Team. Merrimack Energy also reviewed the bids. Subsequently, Merrimack Energy met with the members of the bid evaluation team responsible for each evaluation criteria to compare the results and discuss the basis for evaluation. In all cases it was very obvious that members of Hydro-Quebec Distribution's evaluation team had carefully defined the detailed criteria on which to evaluate each bid within their overall criterion, conducted a thorough and comprehensive review, and prepared detailed documentation to support the results. The result was that "every point" was scrutinized.

6. The non-price criteria were developed to reflect the unique nature of the product sought (i.e. biomass cogeneration).

7. Hydro-Quebec Distribution included all direct purchased power costs as well as system transmission and interconnection costs associated with each bid in Step 2 of the evaluation process, in conformance with the Call for Tenders procedures. This is consistent with the approach undertaken by most utilities in the bid evaluation process, which is designed to include all costs in the analysis.

8. The response to the Call for Tenders was not very robust, with fewer Megawatts ("MW") bid than the level solicited. All eligible bids that met the minimum requirements of the Call for Tenders were selected through the Step 2 process. Due to the limited number of bids, Step 3 in the process was not required.

9. The resources selected were comprised of eight projects, totaling 60.7 MW. One bid was eliminated because its real levelized cost was above the biomass benchmark used for assessing the economics of the proposals relative to market indicators. The benchmark used was reasonable and represented the Feed-in tariff rates for biomass developed and used by the Ontario Power Authority.

In conclusion, it is our view that the approach and assessment undertaken by Hydro-Quebec Distribution is fair, consistent, comprehensive and unbiased. Hydro-Quebec Distribution established procedures and rules which guided the evaluation and selection process, and consistently applied such procedures. The evaluation and selection process was detailed and rigorous. All bidders were evaluated under the same detailed standards and "every point" was carefully scrutinized.