



## Department of Energy

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POWER SERVICES

August 25, 2016

In reply refer to: PS-6

To Regional Customers, Stakeholders, and Other Interested Parties:

On July 18, 2016, the Bonneville Power Administration (BPA) issued a letter informing interested parties that Seattle City Light (Seattle) and Klickitat PUD (Klickitat) requested an early change in their purchase obligation under their Regional Dialogue Power Sales Agreements (Regional Dialogue contract) from the Slice/Block product to the Block product and Load Following product, respectively. BPA included its analysis of the early change in purchase obligation and solicited comments from customers and other interested parties by August 1, 2016. This letter is available at:

<https://www.bpa.gov/power/pl/regionaldialogue/implementation/Documents/#20yrRDcontracts>.

During the comment period, BPA received a total of nine comments from the following customers or customer groups: Franklin PUD, Western Public Agencies Group (WPAG), Okanogan PUD, Emerald PUD, Tacoma Power, Springfield Utility Board (SUB), Clatskanie PUD, Eugene Water and Electric Board (EWEB), and Snohomish PUD. These comments are available on BPA's website at:

<https://www.bpa.gov/applications/publiccomments/CommentList.aspx?ID=307>.

Most commenters were generally supportive of the early product change with the exception of SUB. Several customers, particularly EWEB, Tacoma Power, and Snohomish PUD, tempered their support with requests for additional explanation and analysis on impacts the early product change would have on BPA's rates, risk and operations. BPA has performed additional analysis based on those requests and a summary is included as a separate attachment to this letter. Additionally, the topic of reallocating Slice amounts freed up by the customers' product change to existing Slice customers was also raised by four commenters. In this letter, BPA examines and responds to the issues raised by the parties, and with the additional analysis performed, BPA concludes that both Seattle and Klickitat will be allowed to implement the early product change they have requested starting on October 1, 2017 instead of starting October 1, 2019.

### **Issue 1: Flexibility in Implementing Regional Dialogue Contracts**

SUB took issue with the customers' request to implement a change in products early, saying they did not support BPA working outside of the express terms of the Regional Dialogue CHWM contract, and further compromising the integrity of BPA's own contract structure. SUB favors contractual consistency over flexibility. SUB believes that modifying standard contract terms creates a "most favored" customer situation and disenfranchises customers because it becomes unclear when BPA will allow changes under the contract. In contrast WPAG commended BPA for fostering a business culture of flexibility to meet the evolving needs of its customers and

agreed with the BPA analysis that showed the early product change did not impose added financial risks or create undue cost shifts to other customers. WPAG viewed business flexibility as a strength demonstrated by BPA.

BPA understands both points of view expressed by these parties and remains committed to maintaining the balance established by the Regional Dialogue contracts. However, BPA also remains mindful of the need to provide flexibility to meet its customers' individual requests or needs particularly when a change does not negatively impact BPA's other customers. In addition to the one-time right available to all customers in section 11 of the Regional Dialogue contract, BPA specifically called out the possibility of product changing in BPA's Regional Dialogue Contract Policy ROD of 2008 (Regional Dialogue Policy). BPA noted that it "will remain open to additional product changing on a case-by-case basis as long as it does not shift costs or risks to its other customers."

BPA has previously used a similar public process for an earlier proposed timing change. BPA provided an opportunity to customers and interested stakeholders to review and comment on a change in product purchased when Pend Oreille PUD requested an early change from its Slice/Block product to a Block product. BPA strives to be transparent in its analysis of issues and initiates public processes so that interested parties and others may raise concerns or identify any specific impacts or issues for review and analysis. BPA affords its customers needed flexibility while operating within the parameters of the Regional Dialogue Policy and contracts.

The BPA analysis shared on July 18, 2016, showed no negative impact on other customers for the early product change. Providing flexibility for an early change of two years (one rate period) to accommodate the customers' requests is consistent with BPA's expression in the Regional Dialogue Policy stated above. SUB mischaracterizes the current request by Seattle and Klickitat as utilities unilaterally modifying their agreements with BPA for the purpose of economic benefit; ending its comment with a request that it be allowed a change its purchase amount under the Vintage Tier 2 rate. First, Seattle and Klickitat are not unilaterally modifying their agreements with BPA. This public review of their request is evidence that those customers are not unilaterally modifying their agreements. Second, if BPA were to consider SUB's request and analyze the impacts of such a change it would result in a cost shift to other customers. Therefore, it would be inconsistent with the above expression regarding changing products.

## **Issue 2: Issues Raised around the Tiered Rate Methodology**

Tacoma Power questioned whether there would be cost shifts due to the customers' early product changes and requested that BPA verify its assertion of no anticipated cost shifts by running the BP-16 Rate Analysis Model (RAM) using the assumption that Seattle and Klickitat were purchasing their newly requested products and comparing the results. Tacoma Power's proposed analysis would not simply entail a rerun of RAM. The request would also require BPA to rerun many of the models that produce the inputs to RAM – specifically BPA's hourly hydro model (HOSS); the Loads, Obligations, and Resources Analyzer (LORA) model; the Revenue Simulation model; and Transmission Expenses for Power. The amount of staff time associated with such analyses would be a significant unanticipated workload for BPA.

Workload aside, the expected results of Tacoma Power's proposed analysis would not further demonstrate product choice equity or a cost shift occurring. BPA and the customers developed the Tiered Rate Methodology (TRM) to assign costs to the correct rate pool based on costs for each product. BPA asserts that equity between products is inherent in both the rate pool and cost assignments as part of the design of the TRM. The TRM is designed so that whatever product a customer chooses to purchase, regardless of load shape, substantial cost shifts would not occur since the TRM identifies and assigns all major costs including any costs arising from a change in product to the applicable rate pool for the product. This design that equitably assigns costs through the TRM allows BPA and customers to remain largely indifferent to individual customers' product choices.

In evaluating potential sources of cost shifts associated with Seattle and Klickitat's early product change, BPA looked at the differences in characteristics between the products, such as purchase shape, secondary energy treatment, and applicability to BPA's risk mechanisms. BPA found that these substantive product differences are each identified and addressed through the rate design adopted with the TRM. One potential exception was how BPA looked at capacity charges between the products associated with the amount of capacity grandfathered under each customer's Regional Dialogue contract. BPA recognized that there is a broad range of demand charge impacts for customers depending on their initial load characteristics, to the extent a load might have changed over time and, finally, that a customer changing products might shift costs to others based on the impacts of the demand charge. Because Seattle will purchase at a flat hourly rate during heavy load hours, BPA determined that those potential inequities were not material for a customer that selects a Block-only product, like Seattle has done. In addition, BPA found that Klickitat's change to the Load Following product showed no cost shifts because the charges they will face for demand are in the normal range of how the demand charge impacts other customers with the Load Following product.

As explained in the analytical portion of BPA's July 18, 2016 letter to the region regarding early product change and the open comment period, BPA has identified one instance of potential cost shifts that would apply if Seattle and Klickitat change products two years early. Such potential cost shifts are due to the timing peculiarities caused by Regional Cooperation Debt actions and the corresponding effect those peculiarities had on the Slice True-up in BP-14, and the corresponding proposed commensurate treatment for non-Slice sales in the upcoming BP-18 BPA rate case. Both Seattle and Klickitat have been informed that they would be required to true-up any such cost shifts as part of the early product change process. If other issues are identified, they will be addressed in future rate cases with an intent to ensure that there are no undue costs shifts caused by customers that switch products.

### **Issue 3: Issues Raised around System Operations**

Snohomish PUD questioned whether BPA's peak load forecast analysis using actual Slice load data was adequate because it was only based on FY 2015, which was an El Niño year with unseasonably warm weather and reduced annual and peak loads. Snohomish PUD suggested using a multi-year average of Slice load data based on a minimum of five years. At Snohomish PUD's request, BPA performed additional analysis using a multi-year average of Slice load data,

while excluding Idaho Falls since they have decided not to change products. Due to limited data accessibility, BPA used data from the 39-month period of May 2013 through July 2016. This period spans a majority of the 46 months of operation that have transpired since the Slice Computer Application was developed and implemented in early October 2012 as outlined in the Regional Dialogue contracts. The impact of expanding the data set from the single-year case (FY 2015) to the multi-year-average case (39-months), and removing Idaho Falls, was generally lower coincidental peak loads in the fall and winter months and higher coincidental peak loads in the spring months. BPA views these impacts as small and manageable. They are also well below the 300 MW materiality threshold BPA had originally set, where impacts might need additional consideration.

Snohomish PUD also requested that BPA analyze the aggregate impacts on total monthly peak loads in FY 2018 for just Seattle and Klickitat. BPA performed additional analyses that quantified the impacts under all four Slice assumptions studied for the original product change requests. BPA performed the analysis requested by Snohomish PUD in a similar fashion to the updated FY 2020 case, including using actual Slice load data from the same 39-month data set described in the prior paragraph, and with the analysis only including Seattle and Klickitat. The largest increase in monthly peak obligation was produced by the 1937-critical water scenario, and was 125 MW in both the FY 2020 and FY 2018 analyses.

Snohomish PUD also requested an analysis to quantify the range of possible impacts on the Oversupply Management Protocol due to changes in the customers' purchase obligations. In response, staff further considered the potential impacts a product change has on oversupply. Staff determined that product changes of Seattle, Klickitat, and Okanogan PUD would likely have no impact on oversupply or, at the very most, would be de minimus in nature. The staff analysis recognized that a customer's product choice would not change the regional total load and resources balance mix, nor would it impact the choice of generating resources online during an oversupply event. Any decision of resource operators to run those resources would still be determined by the economics of the market clearing price or bound by operational constraints that remain unchanged under either product choice. Regardless of product choice, oversupply costs are situational, and were last incurred in 2012. Those costs are expected to decrease significantly with expiring production tax credits, expiring Power Purchase Agreements, and the anticipated migration to other Balancing Authority Areas of roughly half of the wind fleet presently located in the BPA Balancing Authority Area.

#### **Issue 4: Should BPA Reallocate Slice Amounts Unused due to Product Changes?**

Emerald, EWEB, and Clatskanie asked BPA to consider reallocating Slice amounts that are vacated by Slice customers moving away from the Slice product. Okanogan PUD specifically opposed reallocation of Slice to existing Slice customers. They asserted that a Slice reallocation would be fundamentally unfair to them since their product change decision has assumed no reallocation, and a decision to reallocate would alter their election to change away from the Slice product. Okanogan PUD's assertion is based on, and consistent with, the existing Regional Dialogue Policy on the Slice product. In BPA's first letter to the region on product changing, issued on June 15, 2016, BPA stated that the reallocation of unused Slice amounts to the current

Slice customers is not provided for by the contract, policies, and records of decision from Regional Dialogue. BPA would have to revise its policy through public processes and changes to the contracts, and BPA has no obligation to do so. As noted earlier, BPA's policies specifically state we would consider product change requests on a case-by-case basis. As we did with the request for Pend Oreille PUD, BPA considers implementing a policy change such as an early product change, when it is convinced that customers are unaffected by, or better off, if the policy change is made. BPA does not believe that would be the case in reallocation of Slice amounts to existing Slice customers. Specific areas BPA considered are discussed below.

#### *Not Linking Slice Reallocation and Early Product Change Process*

Emerald asked BPA to engage in discussion of reallocation of Slice before granting the early product change request. It noted that absent the discussion, they had no way to determine what value the reallocation would have for them. Reallocation of Slice amounts to existing customers was not a part of the Regional Dialogue Policy or contract terms. The value of a nonexistent choice is zero because that choice was never provided for by the Regional Dialogue Policy or contracts. Slice issues from the design of the product to the amounts a customer could purchase were raised, discussed and decided in the Regional Dialogue Policy and the contract negotiation process with BPA customers, prior to offering contracts. BPA considers reallocation of Slice amounts to existing Slice customers to be a fully separable issue, not previously raised, and doing so would require a major change in direction and policy. Further, reallocation is an issue distinct from and beyond the scope of the early product change question. BPA will not propose this change in policy and will not link the two issues.

#### *Negative Impact of Reallocation on BPA Risk and Flexibility*

EWEB and Clatskanie both expressed concerns about the changes in cost risks that could occur due to BPA selling a smaller amount of the Slice product. Their comment focused on the possible impacts that not reallocating Slice to existing customers could have during the spring run-off due to BPA being responsible for managing larger federal power generation volumes. Further, EWEB felt that reallocation would mitigate the potential for cost and risk shifting between customers with different products.

BPA is charged by statute with marketing all federal power from the Federal Columbia River Power System (FCRPS), including surplus power. BPA has marketed federal power for 75 years and has sold a limited amount of Slice for 15. Slice is only one of the products that BPA markets. The amount of Slice sold does not change the amount or shape of federal generation on an annual basis since BPA sells surplus power to Slice customers on an advanced planned basis. Reducing the amount of federal power BPA sells as Slice alters the shape of the federal power that BPA provides to meet its other energy and peak load obligations and increases the flexibility available to BPA for secondary marketing.

In any operating year, there is a potential for BPA's spring marketing to see a higher volume of generation, but EWEB and Clatskanie's assertion that it embodies a greater risk is a narrow view of the federal system risk. For example, since Slice is sold in part as an annual percentage of system capability, additional amounts of Slice retained by BPA due to product changes may

mean higher potential volume in the spring but it may also mean BPA will have additional volume and flexibility in high value times like summer and winter. Additionally, retaining system capability by not selling more Slice, provides additional shaping capability to meet loads and aids BPA's secondary marketing on behalf of all of its non-Slice customers. Even in the spring, the risk mitigation of selling Slice to customers is of limited value because the amount of power that must be sold from the FCRPS is constant, whether marketed by BPA or Slice customers. During extreme circumstances where there is no surplus market, BPA has found that Slice customers are sometimes leaving some of their surplus energy in the system for BPA to manage rather than sell it themselves in a low or negative market. BPA believes that the general equity established in the TRM ensures that customers pay a fair share of the BPA costs regardless of the product they purchase. Issues associated with the shape of the system and value inherent in different time periods will continue to be properly discussed, and accounted for, in BPA's power rate cases.

Finally, BPA recognizes that any question or policy regarding reallocation of Slice amounts to existing Slice customers is closely related to challenging regional conversations between Slice and non-Slice customers about how much Slice BPA would offer. When BPA settled on a maximum of 27 percent of its Tier 1 system planned capability that would be offered in the Slice product, many customers asked that less be offered and the region was mixed in its views over the best amount. Non-Slice customers, notably Northwest Requirements Utilities, were concerned about the sales of BPA system flexibility to an individual customer and were more comfortable with BPA selling less of the Slice product and retaining more of the flexibility to deal with changes in load shapes and other uncertainties as they come up.

The sale of Slice, which is indexed to system capability, creates some operational uncertainty for the FCRPS because customers have rights to a contractually-allowed range of federal system output they can use to meet their load and secondary marketing. That use can change up to 30 minutes before deliveries, and BPA has to manage the federal system to account for this range of operational uncertainty. Reducing Slice reduces that federal system operational uncertainty and allows BPA to incorporate the additional system capability into decisions on how to meet its obligations and optimize value between longer and near-term markets. In addition, because current Slice customers have some of their net requirement load met with Block purchases, a BPA decision to reallocate Slice to a particular customer would result in a corresponding reduction to that customer's predictable, flat monthly Block purchase, and thus would trade a fixed and known power service for additional Slice operational uncertainty.

*BPA Decision Not to Reallocate Unused Slice.*

Although some Slice customers desire additional Slice amounts, the amounts available under the Regional Dialogue Policy and the Regional Dialogue contract to each customer were carefully considered and set by the current contract. No obligation was undertaken to reallocate Slice to existing Slice customers. Fundamentally, BPA does not find that reallocation of power products beyond the obligation stated in the Regional Dialogue contracts, including unused Slice, compelling enough to readdress or reopen the longstanding question of how to allocate and account for system flexibility. BPA believes system flexibility is more important now in 2016

than it was in 2008 when the Regional Dialogue contracts were put in place. Given the continued uncertainty on resource and demand response integration; the changing structure of Western markets; changing load shapes of BPA customers; and future operations under Biological Opinions, BPA is challenged with complex system operations and the responsible marketing and use of federal system flexibility. BPA believes it is best that a new policy direction not be undertaken. The additional federal system capability and flexibility from returned amounts of Slice should be retained to meet the needs that these challenges pose and be managed by BPA for the benefit of all of its customers. Slice customers will continue to receive the same share of value either through their products or the financial impact on the rates associated with their Block purchases. This would be a contentious issue requiring adjustments to the Regional Dialogue Policy, the Regional Dialogue contracts, and possibly to the TRM.

### **Decision to Allow Seattle and Klickitat to Change Products in FY 2018**

BPA appreciates the comments that were provided about Seattle and Klickitat's requests to change products early. Franklin PUD, WPAG, and Okanogan supported the proposal; Emerald PUD and Clatskanie PUD were generally supportive; EWEB, Tacoma Power, and Snohomish PUD conditioned support upon additional analysis; and SUB did not support the proposal. The issues discussed above under sections 1, 2, and 3 respond to the concerns and proposals that were raised and explain the additional analysis undertaken based on the comments received. BPA believes that the additional analysis and explanations provided address the customer concerns and meet the conditions for support established by EWEB, Tacoma Power, and Snohomish PUD. After considering the issues that were raised on an early product change and conducting the further analysis noted above, BPA finds that no significant operational or other unanticipated impacts are created by an early product change by Seattle and Klickitat. Therefore BPA has decided to grant the request.

BPA will allow Seattle and Klickitat to change their purchase obligations from the Slice/Block product to the Block product and Load Following product, respectively, effective on October 1, 2017. BPA will offer Seattle and Klickitat amendments to their Regional Dialogue contracts, replacing all terms for the Slice/Block product with the standard Block product and Load Following product terms, respectively. If you have any questions, please contact your Power Services Account Executive, Scott Wilson at (503) 230-7638 or myself at (503) 230-5175.

Sincerely,



Garry R. Thompson  
Vice President of Requirements Marketing